OCCASIONAL PAPERS: 6

RECONSIDERING CO-OPERATIVES: LESSONS FOR MALTESE CO-OPS

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FOREWORD

The series of *Occasional Papers* published by APS Bank promotes discussion of economic and social issues. *Occasional Papers: 6* collates theoretical considerations and direct experience with regard to a social model of organisation, Co-operatives. The publication extends the discussion launched in a seminar organised by APS Bank in 2004 entitled "The Future of Co-operatives in the Agriculture and Fisheries Sectors". The Proceedings of that seminar are in print in English and Maltese.

Co-operatives dominate the sector of agriculture in the Maltese Islands, but they are not restricted to that economic activity only. A lot was expected of them in the running in to Malta's membership of the European Union. But as the various speakers pointed out during the 2004 seminar, the co-operative model leaves much to be desired as regards the delivery of timely change in members' attitudes, institutional structures, and operational tools for the required predisposition to strive for economic efficiency in the Single Market of the Union. The versatility needed to compete is even more urgent in the context of a revamped Common Agriculture Policy and a relatively freer global trade environment.

Occasional Papers: 6 presents six papers, organised in two parts. Part One examines legal and economic issues. Lawyer David Fabri highlights the main features of legislation regulating co-operatives in the Maltese Islands and draws a comparison between co-op and company laws. It is a relevant starting-point for any meaningful discussion of co-ops in an enlarged European Union that is striving to streamline such legislation across the European economic space. The undersigned examines the underlying economic and ethical (solidarity) rationale that supports the co-operative institutional model and draws lessons for Maltese co-operatives. These co-ops have failed to provide strong leadership and technical support, and so insights into the strengths and weakness of the co-op model itself may be conducive to the survival of this institution. Besides, research into long-term sustainable economic growth emphasises the role that institutions have in such a process. Hence it is in everybody's interest that organisations induce and, in turn, respond effectively to changing economic and social conditions.

Part Two presents examples of every day realities and structures. John Rowse and Janos Juhasz, former officials at the Food and Agriculture Organisation of the United Nations, examine the experience of co-ops based on a world wide review of such organisations. There is a lot to assess in such an overview of realities and the support that successful co-ops demand in order to be operationally fulfilling. John Millns, who supervised a Technical Co-operation Programme for Maltese co-operatives, presents his views on the strengths and weaknesses of such co-ops as well as proposals for future development. He also co-authored a Case Study on the Poultry Sector – and the role of the Poultry Co-op – with Egon Samler. Kyriacos Patsalos, a former Senior Agriculture Officer in the

Department of Agriculture, M.A.N.R.E., Cyprus, delves on the lessons learnt from many years of activity related to the setting up of Producer Organisations in Cyprus. Producer Organisations are a pre-requisite for the support structures in the Agriculture and Fisheries sectors in the European Union, beside other forms of support that national governments may undertake. So learning from the experience of successful set-ups is always positive and useful.

The views of the contributors are solely their own. They do not reflect the opinion of the institutions to which they are, or had been, attached. APS Bank presents this collection of articles in order to stimulate debate on the topics examined. APS Bank has no corporate view on these subjects.

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January 2006

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E. P. DELIA, Chairman of APS Bank Ltd, spans academic research/ teaching and public sector policy formation and business decisions. He has published widely in the areas of demography, labour markets, trade and fiscal policy in the context of economic development in the Maltese Islands. Recent publications include the titles issued under the APS Bank Occasional Papers Series, 1 to 5; *Towards Sustainable Welfare Programmes and Pensions in Malta* (1998); and *Papers on Malta's Political Economy* (2002)

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JOHN ROUSE is a graduate of the Universities of Virginia and Wisconsin in the USA. He has worked on a Consultancy Basis for the World Bank, as Agricultural Economist for the World Council of Credit Unions and on a full time basis with FAO as a Senior Officer (FAO) Co-ops and Rural Organisations. During this term of full-time employment with FAO he played an active role in the development of the FAO Plan of Action on People's Participation in Rural Development. Although he has retired from full-time employment he is still an International Consultant for FAO and IFAD.

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EGON SAMLER is a graduate of the Agriculture Faculty, Rehovot and the Polytechnic Institute, Haifa. He is the former Head of the Animal Husbandry Department & Poultry Division in the Ministry of Agriculture and Rural Development of Israel. He has a wide ranging experience in activities related to the poultry sector. He was sent to Malta by FAO to report on the Poultry Industry as part of the TCP Project on Co-ops.

KYRIACOS PATSALOS has a long career in the Agriculture Sector. He obtained his B. Sc. in Agriculture from the Athens Agricultural University and his M. Sc. in Whole-Plant and Crop Physiology from Reading University (UK). He also followed training programmes in Holland and the U.S.A. Up to the end of November 2005 he was the Head of the Horticulture Section in the Department of Agriculture in Cyprus and was responsible for the implementation of CMO of the Fruit & Vegetable Sector. He was also in charge of the enforcement of the Law on the recognition and operation of Producers Group and Producers Organisations in Cyprus. He successfully formed twelve POs which are all functioning efficiently. Mr Patsalos has recently resigned from Government Service and formed his own Advisory Company.

PART ONE

CO-OPERATIVES – COMPARATIVE LAW AND ECONOMIC FOUNDATIONS

DAVID FABRI

THE CO-OPERATIVE SOCIETIES ACT 2001 - A COMMENT ON THE RECENT REFORMS IN MALTESE CO-OPERATIVES LAW

Scope of the Paper

The principal legislation governing co-operative societies in Malta is the Co-operative Societies Act which was passed by Parliament in 2001. It was brought into force in stages the following year. The 2001 Act has repealed and replaced the co-operative legislation that preceded it, namely the Co-operative Societies Act 1978. This recent reform and the introduction of new legislation for co-operatives offers, in the view of the writer, a timely opportunity for a fresh look at the subject of co-operative law, and how co-operatives in Malta are or should be regulated in the 21st century.

This paper reviews some of the main features, innovations and improvements in the new Act and offers a brief analysis of the significance and impact of the transition from the now repealed Act of 1978 Act to the 2001 Act. It attempts to place this transition within the context of other recent developments in Maltese corporate law especially the adoption of the Companies Act of 1995. Highlighting certain elements in the legislation that tend to be overlooked, the paper explores the motivation behind the recent reforms. This exercise should throw light on how legislative and regulatory policies regarding co-operative societies have matured and are still evolving.

It would be unrealistic to attempt to describe and analyse all the many new provisions and concepts contained in the new Act, or to investigate all the various policy and practical implications. A full and comprehensive analysis of the entire Act and its background would have warranted more time and space, indeed an entire text-book. The aim here is less ambitious, but it shall try to show that the law governing local co-operatives is worthy of analysis and study in its own right. The paper may hopefully also furnish some useful groundwork for other studies on co-operative law and practice in Malta.

In order to remain within manageable limits, this paper mainly focuses on the Act itself, its backdrop and the broader issues, and does not analyse in any detail the regulations issued under it. Some important regulations have indeed been issued concerning such matters as the administration of the Central Co-operatives Fund and the imposition of administrative penalties. Moreover, the comments on the new accounting and reporting obligations and on the special processes governing the registration and incorporation of co-operatives and their dissolution and winding up are brief and certainly incomplete.

On the other hand, the paper could not have avoided at the least a preliminary and tentative (but hopefully meaningful) comparison between current co-operative law and company legislation. The most obvious corporate rival to the co-operative model is the limited liability company. The private company vehicle has proved a runaway success, a true motor of the local economy. Rightly or wrongly, the co-operative form is regularly measured against the company model. Accordingly, a significant part of this paper is dedicated to this field of enquiry.

A very brief and selective historical note

How did the 2001 Act come into being? It may be useful to take a brief (and admittedly sketchy) look back. In the years prior to 2001, unspecified legislative changes to the Co-operative Societies Act, 1978 had been periodically promised by various official sources.

An early and quite comprehensive ten-page study was published by the Co-operatives Board in November 1993 as a "Proposed Policy for the Development of Cooperatives in Malta". The document stated its purpose as *"intended to highlight the need that a new impetus be given to the Cooperative Movement in Malta. While it is a formulation of policy objectives, it is by no means intended to place the movement and the Central Cooperatives Board in a straight jacket. It should rather serve to provide an inspiration for future initiatives and possibly for legislative reform in this area."*[1]

A Sunday Times report of 14 July 1996 covered an address by the then Environment Minister, Dr F Zammit Dimech, headed "*Growing interest in cooperatives*". A few days earlier, the then Parliamentary Secretary Dr Joseph Cassar had been quoted as saying that *"The cooperative movement is gaining ground in Malta as its members and productivity increases steadily"*.[2] More significantly, Dr Cassar also gave notice that *"legal reform to bring legislation up to date is in the pipeline"*. On the 5 July 1998, the Independent on Sunday reported that "*Social Welfare Minister Edwin Grech expressed the hope that the draft bill of the amended Cooperatives Law will be ready by the end of 1998. These will be the first changes to be effected in the law since it was passed by Parliament in 1978.*".

On the 18 January 1999, a Times report headed "*Government planning to upgrade cooperatives law*", reported the then Social Policy Minister Dr L. Gonzi as saying that *"the law on cooperatives…had remained unchanged for the past*

25 years and had not been adapted to tackle today's challenges."[3] A new law was eventually drawn up, published and presented to Parliament.

The Co-operative Societies Act 2001 is the third legal instrument passed in the course of this century specifically aimed at establishing a suitable legal framework for the formation and operation of co-operatives. The three enactments are:

(i) **The Co-operative Societies Ordinance of 1946**
This was introduced by Ordinance No. XXXIV of 1946, adopted on the 8 July 1946 and brought into force on the 12 December 1946. Its stated purpose was "*to provide for the constitution and regulation of cooperative societies*".

(ii) **The Co-operative Societies Act of 1978**
This Act was listed as Chapter 278 of the Laws of Malta and was brought into effect on the 16 April, 1979. Its stated purpose was "*to provide, in place of the Co-operative Societies Ordinance, 1946, for the constitution, registration and control of co-operative societies and for matters connected therewith…*".

(iii) **The Co-operative Societies Act of 2001**
This more recent Act describes itself as "*An Act to provide for the constitution, registration and control of co-operative societies and for matters connected therewith or ancillary thereto*." It is listed as Chapter 442 of the Laws of Malta.

Originally, the intention was to revise, improve and update the provisions of the 1978 Act, not to replace it. It was felt that a limited exercise, capable of being undertaken within a reasonably short time, would have sufficed at that stage of co-operative development. Had the original intention been that of creating a brand new Act, a formal policy white paper would probably have been published to accompany the beginning of the drafting exercise.[4]

At various stages during 1998-2000, following some initial studies and consultation, a number of specific areas were being identified as ripe for revision and updating. The 1978 legal framework had been the point of departure for the enterprise. Eventually, as the drafting work proceeded, and as new ideas flowed, the proposed amendments started to gradually take shape and seemed to assume a life of their own outgrowing the confines of the 1978 Act. The Act no longer guaranteed a suitable platform for the extensive reforms that were maturing. A new framework was needed to house them coherently. A decision was soon taken at ministerial policy level to formulate the proposed changes in the shape of a brand new Act, and have them presented to Parliament accordingly.

Although the 2001 Act is for all purposes a new law, its construction relied heavily on the 1978 Act. While introducing significant improvements and several new elements, there was concern to safeguard continuity. In the writer's view, the new Act does not constitute a complete break with the past. It does however represent a fresh start and a relevant new landmark in local co-operative history. The shift towards replacing rather than amending the 1978 law certainly presented a wider opportunity to re-appraise old concepts and mechanisms and to contemplate and implement new ideas and solutions.

The Constitutional Context

The Constitution and co-operatives in the same sentence. The Constitution is where all law acquires its legitimacy. It is the basis of legality in our country, a document which establishes the different arms of the state and which assigns legislative authority to Parliament. Chapter 11 of the Constitution sets out a *"Declaration of Principles"*. This occupies articles 7 to 21 of the Constitution. These principles are described as *"fundamental to the governance of the country"*. Article 20 lists the *"encouragement of cooperatives"* as one of the fundamental principles to which the State must adhere. The full statement is: *"The State recognises the social function of cooperatives and shall encourage their development."*

Regrettably, these principles are not so fundamental as they may not be enforced in a court of law,[5] although it remains a duty of the state to *"apply these principles in making laws"*.[6] This official recognition of the social importance of co-operatives in the highest law remains significant despite its non-enforceability.

Arguably, these principles seem to reside in a kind of no man's land, simultaneously law and non-law. On the one hand, they carry moral authority and provide a useful expression of intent and values. On the other, they offer a potentially negative precedent and a legal hodgepodge seeing that it is of the essence of law to be binding and to create rights and obligations.

Returning to the co-operative context, an analogous question arises. A new formulation has been articulated for the re-stated Co-operative Principles (see further below) under Part III of the 2001 Act.

A Legal Framework for Co-operatives

The Co-operative Societies Act of 2001, like the 1978 Act before it, applies to all co-operatives seeking to establish themselves in Malta. It governs the establishment, legal status, management and dissolution of co-operative societies in Malta, whatever their activity or membership. Although not as detailed and voluminous as the Companies Act,[7] it is still quite a comprehensive law which manages to deal with most important issues.

A co-operative is a form of business organization recognized and supported by law. It is an artificial legal person, enjoying legal personality created by operation of the law following registration by a public authority. Registration leads to incorporation and the creation of an autonomous new subject capable of suing and be sued, of acquiring and holding property, entering into contracts, engaging employees, opening and operating bank accounts, etc.[8]

The 2001 Act primarily seeks to regulate the use of the particular vehicle or medium of the co-operative. Unlike such laws as the Banking Act and the Insurance Business Act, its main object is not to regulate a particular sector of business or professional activity. The 2001 Act sets out a revised updated framework to govern the formation, the management and the closing down of co-operatives, without revealing any particular interest in the actual underlying economic activity undertaken by the societies themselves. With this approach, the Act has shifted closer to company law. Co-operative and company law share a common concern to restrict the abuse of the corporate form and to promote minimum good governance standards. Beyond these concerns, they are broadly reluctant to delve into the actual commercial activities carried out by the entities they regulate.

The Co-operative Societies Act of 1978 disclosed a more evident interest in the underlying economic performance of registered co-operatives. In fact, the 1978 Act required the Board to monitor how registered co-operatives were actually performing and to offer them assistance. The Board was also specifically called upon to try *"to help cooperative societies to increase their efficiency"*,[9] a requirement which does not feature in the recent 2001 Act or in company law.

The Transition from the 1978 Act to the 2001 Act

When the new Act was being designed, steps were taken to ensure that business could carry on as usual without any unnecessary disruption. This is an issue which always needs to be tackled with care whenever a particular legal framework is being altered, and especially when an entire law is being replaced. In these instances, one is bound to find what are often referred to as *transitional* arrangements. These would explain when, how and to whom the new provisions would apply. The Co-operative Societies Act 2001 was brought into force on the strength of Legal Notice 49 of 2002. The transitional arrangements were laid down in some detail in the same Legal Notice[10], which brought the Act into force in three stages. All the articles of the new Act are now in force.[11]

With the adoption of the Co-operative Societies Act 2001, the 1978 Act was repealed.[12] None of its provisions remains in force and it is now consigned to legal and co-operative history. The new Act contained in-built mechanisms to guarantee the full legal and practical continuity of the Co-operatives Board and of the co-operatives already registered and operating under the previous law.[13] This step ensured that no needless uncertainties or gaps would be occasioned by the legislative changes, and the business operations of registered co-operatives continued smoothly and suffered no disruption. All the decisions and actions taken by the Co-operatives Board under the old Act were safeguarded and were retained in force. This rule extended to all administrative and other measures adopted by the Co-operatives Board prior to the coming into force of the new law.

Some of the changes introduced in the new law necessitated a small number of amendments to the statutes of existing societies. These amendments reflected a number of options that the new law has allowed each society to adopt. The new law allowed co-operatives to choose from a number of alternative arrangements and gave them sufficient time to pass the necessary amendments. This marked a departure and an improvement from the 1978 Act which envisaged only one relatively static and rather restrictive co-operative structure. This new approach offers more flexibility for co-operatives to determine their internal structuring. It allows big and small societies to adopt arrangements more suitable to their size, resources and needs.

The changes also meant that freed from the one-model approach, co-operative societies now need to give much greater attention to the correct formulation of their statutes. They cannot rely any longer on the one-size-fit-all model at the core of the 1978 Act. Co-operatives now need to take several sensible fundamental decisions on how they wish to operate and to regulate their internal procedures. This is the small price existing co-operatives have had to pay in order to gain more flexibility in their internal arrangements as a consequence of the new law. In reality, only a few adjustments to existing statutes were required.[14]

Revisions to the statutes became necessary due to the new or revised concepts, obligations and possibilities made available by the new Act. It would be useful at this stage to identify some of the various options that may now be exercised by a co-operative society in the preparation of its statute:

(a) it may establish a Supervisory Board;
(b) it may provide for the duration of appointment of members on the Supervisory Board;
(c) it may provide that the members of the Committee of Management retire by rotation and may provide for the election of runners-up;
(d) it may provide for certain restrictions on members' activities and may impose penalties for breaches thereof;
(e) it may impose penalties for infringement of the statute;
(f) it may contain rules on conflict of interest and competition;
(g) it may allow meetings to be held electronically;
(h) it may refer disputes to Malta Arbitration Centre;
(i) it may state maximum rate of dividend payable to members;
(j) it may allow commercial partnerships to become members of the society;
(k) it may establish special qualifications for membership;
(l) it may provide alternative rules on voting rights;
(m) it may require that a motion for the dissolution of a society be confirmed at a second general meeting.

Co-operative Principles – An Enhanced Status

One of the most striking innovations in the new Act is the re-statement and elaboration, in new article 21, of the seven core principles of co-operative existence. These principles set out the major underlying philosophical thinking behind the provisions of the Act itself. They clearly originate from the original principles defined and adopted in 1966 at the 23rd Congress of the International Cooperative Alliance. The law does not expressly refer to the ICA, but the origin is very evident.[15] Originally mentioned in an unduly telegraphic shape in article 11 of the 1978 Act, these principles have now been articulated in a more forceful and detailed manner. They are now better equipped to highlight the major concerns at the basis of a co-operative society's constitution and activities. In summary, they set out the following core set of values:

(a) voluntary and open membership;
(b) democratic member control;
(c) member economic participation;
(d) autonomy and independence;
(e) education, training and information;
(f) co-operation among co-operatives;
(g) concern for the community.

What is the legal status of these core principles? The Act states that they cannot be directly enforced through the courts. So have they too been devised as an unenforceable set of principles enjoying mere moral value on the lines of the Declaration of Principles under article 21 of the Constitution? Fortunately, the answer is likely to be a "*no*", as the Act has taken pains to endow them with a higher status and to make them more effective in practice. The law now requires them to be respected and adhered to by all persons applying and interpreting the provisions of the Act.[16]

Co-operatives and their controllers as well as the Board and its employees are now required to consider these extraordinary principles as fundamental to their policies and day to day co-operative activities. In this sense, it appears safe to suggest that the co-operative principles now enjoy a freshly enhanced status, and are certainly no longer a vague *mission statement*. Whether this is sufficiently understood or applied in practice is of course a moot point. It would be interesting to gauge whether and how far these guiding principles effectively influence and inspire the daily workings and decisions of co-operatives and of the Co-operatives Board.

Selected new features of the 2002 Act

Space does not permit a complete identification and analysis of all the changes and new concepts introduced in the new Act. Still, this paper cannot fail to highlight some of the interesting features in the recent co-operatives law and to briefly comment on their implications. What follows is a personal and selective list.

Competition law

A complete novelty, article 40 of the new Act is where co-operative law meets competition law. It attempts to resolve the possible conflict that may arise between the law governing fair competition, anti-cartel and restrictive agreements on the one side, and co-operative statutes and agreements with members-producers on the other. Certain restrictive agreements are often entered into between competitors and suppliers within a co-operative society. This article seeks to establish a sensible balance between safeguarding certain societies' core objectives and operational requirements, and respecting the restrictive framework of the Competition Act of 1994[17] and, since 2004, the competition rules of the European Union.[18]

The 1994 Act treats all business and professional undertakings equally and makes no concessions to co-operatives. New article 40 *inter alia* tests the legitimacy and compatibility of such co-operatives rules and agreements on the grounds of necessity, proportionality and reasonableness and the need to safeguard the *"proper functioning of the society"*.[19]

The Apex Organization

The 1978 Act provisions regarding the Apex organization were patchy and inconveniently scattered throughout the Act. These have now been consolidated and presented much more coherently in Part X of the Act, which now makes more convenient reading. This tidying-up exercise has removed certain doubts that had arisen under the 1978 Act, particularly as whether it was strictly necessary for the Apex itself to assume the form of a co-operative. Having been a co-operative, under the 1978 Act, its internal organs and management had to be structured accordingly. It also fell under the regulatory supervision of the Board in every respect,[20] giving rise to an anomalous situation.

The new Act now describes the Apex as a voluntary association.[21] It requires the Apex to represent a majority of registered societies. This means there may only be one Apex organization, reflecting another clear policy decision. On the strength of such a mandate, the Apex could legitimately serve as the most important point of reference, lobby and voice for the co-operative movement. Articles

106 and 107 define in some detail the procedures for the recognition of the Apex by the Board, including a number of basic formal requirements that it needs to satisfy. The Apex organization is today a member of the International Co-operative Alliance.

The role of the Minister

Various provisions of the 1978 Act handed discretionary powers of intervention to the Minister politically responsible for co-operatives. More enlightened thinking criticized these powers as troubling and unacceptable. In the new Act, the Minister's intrusion in co-operative matters has been greatly curtailed, with most of the offending provisions either withdrawn or suitably trimmed.

Article 20(4) allowed applicants to appeal to the Minister from a Board decision rejecting an application to register a society. Article 26(8) of the 1978 Act allowed an appeal to the Minister from a Board decision rejecting a proposed amendment to a society's statute.[22]

Articles 109, 110 and 102 of the 1978 Act elevated the Minister to the position of final arbiter over certain classes of disputes between parties involved in or with co-operatives. This allowed him to prevail over the Board acting in its regulatory role and put him at par with the Court of Appeal. The law has removed these powers and now seeks to direct these disputes towards arbitration.

The Minister's right to give directions to the Board too has been slightly but significantly re-visited. The relationship between the Minister and the Board is primarily governed by article 8. While largely reproducing the old article 8, it now pointedly requires the Minister to issue his directions *"in writing"*. The Board remains obliged to provide information to the Minister, but now only to enable him to exercise his functions under the Act, and in particular to issue policy directions. The Minister retains his prerogative to appoint the Board[23] and to make regulations on the various matters listed in article 108.

The Malta Arbitration Centre

The new Act[24] specifically mentions the possibility of referring disputes involving co-operatives to the Malta Arbitration Centre.[25] This new approach has replaced the former rule that co-operative-related disputes were to be determined by the Board or (worse) by the Minister. The Act now actively encourages the submission of these disputes to arbitration, seen as a more flexible and low-key method of settling disputes. The attempt to shield co-operative disputes from the ordinary courts (and presumably the general public) was a constant theme running through the 1978 provisions, which perhaps tried too hard to retain such disputes in–house.[26]

Membership

Under the new Act, a co-operative is now required to have at least five members,[27] upon its commencement and also on a continuous basis thereafter. The previous minimum under the 1978 Act was seven members, whereas the 1946 Ordinance originally required at least twelve members.[28] This change was intended to facilitate the establishment of very small co-operatives. These small undertakings may now also opt to do without a supervisory board, thereby resolving another difficulty that small societies encountered under the former law.[29]

Another innovation is the introduction of specific rules governing the holding of shares in a co-operative society by a company or other commercial partnership. New article 53 (2) lays down conditions and restrictions. An important limitation states that a company (or other commercial partnership) may only hold shares in a co-operative "*where the statute specifically so permits*". Members are therefore free to make up their own minds on this question.

Subsidiary companies

New article 22 (3) now specifically recognizes that within certain parameters, a society may become a *parent society* and establish *subsidiary companies*.[30] The parameters require the subsidiary "*to fulfil, promote, complement or advance the objects*" of the co-operative, to keep it adequately informed of its activities and to take into consideration its wishes. This new rule seeks to extend, in a sensibly restrained manner, the range of commercial opportunities and arrangements that co-operatives can now enter into, an underlying motive behind several changes introduced in the 2001 Act.

Conversions

It has now become, at least on a conceptual level, possible to convert a co-operative society into a commercial partnership, and vice versa. The precise legal mechanism to enable either process to happen has not yet been provided. Indeed, article 108 (4) foresees the issuing of regulations by the Minister for this purpose. The article makes a reference to the relevant articles in the Companies Act, which however do not yet permit or recognize the conversion of a commercial partnership into a co-operative or other entity not regulated by the Companies Act. This means that appropriate amendments to the Companies Act would have to precede the issue of any such regulations.

Public sector co-operative schemes

Public sector co-operatives present particular characteristics.[31] A few societies had been registered under the 1978 Act, which however did not specifically recognize them. In certain respects, their status under that law raised a few doubts. For the first time, the 2001 Act specifically refers to them. The law has tried to clarify their legal position, thereby removing the uncertainties regarding this category of co-operatives. They are now specifically recognized as a special category of co-operatives and are – to a degree – regulated differently. Article 29 (3) describes them as "*Societies set up in accordance with co-operative schemes developed by government for public employees*" and requires the Board to have them registered separately from other societies. The Minister is also empowered to issue regulations to govern (and to lengthen) the duration of their provisional registration.[32]

Internal Management

The Act, like the 1978 Act, regulates in some detail the manner a co-operative is to be internally organised and managed. It lists the various organs which have to be set up and their respective functions, as well as a number of official posts that have to be filled and the respective duties attaching thereto. This means that the law does not allow a society absolute freedom as to how it can organize itself internally. In this respect, however, the new Act allows greater space and scope for alternative arrangements than the 1978 Act.

The Act expects a high standard of performance from co-operatives and their officials. To this end, the law lays down several stringent rules relating to proper record-keeping and the need to adopt proper management and reporting systems and procedures. Proper financial statements are to be prepared annually and submitted to a proper audit carried out by qualified professionals.

As was the case in the previous Act, the Co-operative Societies Act of 2001 lists a number of mandatory posts that have to be filled by society officials. These posts have to carry the specific designations laid down in the Act. Another mandatory requirement is the appointment of an auditor. These posts are mandatory for all societies, without distinction. These are minimum requirements and they do not exclude additional appointments; provided, it would seem, that any additional appointments do not adversely affect the powers and functions of the statutory organs and officials.

Every Co-operative is obliged to make formal appointments to the following posts:

(a) the committee of management[33];
(b) the following officials: a President[34], a Vice-President[35], a Secretary[36], and a Treasurer[37];
(c) the auditor[38].

The new Act has confirmed the requirement for every co-operative to have a **committee of management,** roughly comparable to the board of directors of a company. Its functions are listed in article 74 while its *"Conduct of affairs"* is described in article 76.

These two rules owe their origin to the 1978 Act[39] and constitute a truly inspired piece. These two articles taken together in fact outline perhaps the earliest local example of a minimum corporate governance statement. They lay down a sufficiently well-phrased benchmark of behaviour and performance to be expected from the members of a committee of management. The slightly updated 2001 statement now require members to exercise *"the prudence and diligence of ordinary persons of business"* and to implement *"proper and prudent accounting policies"*. It holds them jointly and severally liable for any losses occasioned through *"failure on their part to exercise such prudence and diligence…"* or through failure to adhere to the statute or the law.[40]

Article 65 of the 1978 Act helpfully described the main functions and powers of the committee of management and has been retained with minimal changes as new article 74. An extraordinary power which the new Act has assigned to the Board is found under Part II which deals with the powers of the Board. This tackles a potential crisis situation, which did occur in practice though rarely, where the committee of management for whatever reason stops functioning or is functioning contrary to the statute or the law. The law has responded to the need that a solution be found to extricate the society out of this impasse which may cost it relevant commercial and financial repercussions. With the regulatory framework now available, one can think of at least two solutions. Ideally, a general meeting of the members should be convened without delay to take stock of the matter, decide the necessary steps, revise the composition of the committee and issue appropriate directives. Where the impasse, as may indeed happen, renders it difficult even to summon a general meeting or to achieve a quorum, the Board may now step in and exercise its new powers and remove and temporarily replace the committee. The appointees shall than be responsible to manage the society's activities and they shall be obliged to arrange the convening of a general meeting for the election of a new committee, even with the moral and logistical assistance help of the Board itself, as may be necessary. These extraordinary powers are only to be used in extraordinary circumstances. The Board would use these powers sparingly and only where all else fails.

The new law has also re-appraised the role and status of the **supervisory board**. The 1978 Act had required every society, irrespective of its size and irrespective of the will or wishes of its members, to set up a board to operate as a second tier of management authority. No similar or equivalent structure is known to our company legislation. Article 78, now discontinued, described the various and surprisingly wide functions of the board.

In practice, small co-operatives often failed to muster sufficient officials to man the board or found it too costly. Local experience also revealed that some societies actually operated (and seemingly well) without a board, although strictly this constituted a breach of the Act. Regrettably, where a functioning supervisory board had been set up, uncertainties and confusion often arose as how it co-existed with the committee of management. It seems that some boards were unable to shake off the temptation to double-guess the committee of management's decisions and attempted to dictate matters to it. One main cause of this overlap was the broad terms in which the board's functions were formulated in article 78.

The new law has sought to restore some order and to reduce the potential for overlap or confusion of roles. One significant and welcome remedy is making the supervisory board[41] no longer mandatory but optional. It is now set up only if it is either required by express provision of the statute; or is required by a resolution of the general meeting.

Where set up, the board is answerable and reports to the general meeting. The board is expected to assist the committee of management *"in the effective and efficient running of the society"*[42] and to monitor the management and to guarantee legality. The board is not there to obstruct or undermine management or try to take decisions in its place. Should the supervisory board wish to send an urgent message to the members on matters falling under its competence, it has been given the extraordinary right to require "*at any time*" the summoning of an extraordinary general meeting[43].

The two-tier management and supervision system under the 1978 Act was unique to co-operatives. On paper, it appeared to offer a sound approach with one level overseeing the other thereby guaranteeing better corporate governance. In practice the system did not work properly and in some cases proved a hindrance rather than an advantage. Most co-operatives were too small to warrant or sustain a double layer structure of management.

Rather than eliminate the supervisory board altogether, policy preferred allowing societies to decide for themselves. In the appropriate cases, where adopted voluntarily, the supervisory board mechanism may still afford significant benefits to societies and their members, now solely responsible for weighing the likely benefits of having a supervisory board against the possible disadvantages.

Following United Kingdom practice, locally registered companies have invariably adopted the single-tier management system consisting of a board of directors. The Companies Act, as did the Ordinance before it, has only ever recognized the board of directors. No suggestion to change this practice has ever been recorded. The board of directors is a mandatory organ under company law as the committee of management is mandatory under co-operatives law.

The **annual general meeting** is established as the supreme authority of a co-operative. In this respect, the law has remained the same.[44] Generally, all members are entitled to attend and vote at the meeting. The first general meeting shall be held within six (formerly three) months of the issue of the certificate of registration. The purpose of this early meeting is primarily to elect the officers of the society as required by the Act[45] as soon as possible. Every society is obliged to hold an annual general meetings and article 66 (broadly equivalent to former article 59) very usefully specifies in detail the matters that such meetings are required to consider. In brief, these include:

(a) the approval of the financial statements;
(b) the appointment of the committee of management;
(c) the appointment of the supervisory board, if any;
(d) the consideration of any proposed amendments to the statute;
(e) the consideration of the auditor's report;
(f) the appointment of the auditor;
(g) the consideration of the distribution of the net surplus;
(h) the determination of the maximum borrowing limit of the co-operative;
(i) the hearing of appeals and complaints in respect of certain decisions of the committee of management;
(j) the payment of honoraria, fees and other remuneration.

The Act also regulates in some detail the procedures to be followed at general meetings, the quorum required and the keeping of minutes. New rules governing the manner of appointing of the committee of management have also been introduced.

The Auditors

The 2001 Act expects a high standard of performance from co-operatives and their officials. To this end, the law lays down several stringent rules relating to proper record-keeping and the need to adopt proper management and reporting systems and procedures. Accordingly, article 48 highlights the obligation of every cooperative to keep *"proper accounts and records of its transactions and affairs"*, to ensure that all payments are *"correctly made and properly authorized"* and that the society's assets are properly safeguarded. Financial statements are to be drawn-up annually. These are to be completed not later than two months after the relative year-end and then submitted to an audit. The reforms in co-operative accounting and audit obligations introduced by the 2001 Act are considerable and have brought co-operatives regulation closer to the company law rules.

In the Companies Act, auditors play an important role in overseeing the keeping of accounts and the verification of corporate financial statements. The same is true of both the 1978 and 2001 Acts. New detailed accounting rules have been introduced in the 2001 Act and the model adopted is the Companies Act 1995. Direct references are made to the application of '*International Accounting Standards*' and of '*International Standards on Auditing*' to co-operatives.[46] A new Third Schedule has been added to the Act explaining the Form and Content of Individual Accounts.

From a historical angle, this development represents a sizeable departure from the practice apparently prevalent under the 1946 Ordinance. In his annual report for 1947-8, (very soon after the Ordinance came into force), the Registrar made some revealing comments. Under the part headed *"Auditing and Supervision"*, the then Registrar, Mr O. Paris, lamented that the newly registered societies lacked accounting expertise: *"all secretaries started their work without any knowledge of book-keeping……."*. As a result, *"The audit of the accounts of all the societies was carried out solely by the staff of the department."*.[47]

The new Act of 2001 has now reduced the auditing role of the Board to a minimum. The 1978 law prohibited an auditor of a co-operative from accepting appointment unless he has been vetted and authorised by the Board. This rule has been removed. The recent amendments have also done away with the previous grandmotherly rule whereby the Board was obliged to vet and approve the fees that an auditor was proposing to charge a co-operative for his services. Under the new Act, any person qualified to act as auditor of a company in terms of company legislation is considered qualified to audit cooperatives.[48]

Article 96 of the 1978 Act was another important rule which has been re-visited. This article, whose origin may be traced to the practice under the 1946 Ordinance, made the Co-operatives Board responsible *"to supervise the auditing of every society"*. Now considered archaic, intrusive and disrespectful to the auditing profession, the rule has been eliminated from the 2001 Act.

The rules governing the status and duties of auditors in the 2001 Act have been updated to take into account recent developments in the auditing profession and in auditing and accounting standards. Article 49 requires the auditor to ascertain whether the Management Board complied with the provisions of the Act, with the statute and with good accounting practice.

Section 41 of the 1978 Act regulated the audit of the financial statements of a co-operative. The auditor was required to confirm *"whether the financial statements show fairly the financial transactions and the state of affairs of the society"*. He was also obliged to report directly to the Co-operatives Board *"any irregularity disclosed by the inspection and audit that is, in the opinion of the auditor, of sufficient importance to justify his doing so"*.

Indeed, the 1978 Act may have been the first law in Malta to introduce a tentative form of mandatory whistle-blowing. Article 41 required an auditor to immediately notify the

Board of any irregularity resulting from the audit which *in his opinion* was important enough to justify this action. Article 49 of the new Act has been articulated differently. It now requires an auditor to *"forthwith inform the Board and the society or any of its officers of any material irregularity disclosed in the course of his audit"*. The purely subjective test established by the 1978 Act has been replaced by a broader and more objective test. The new Act, in its re-formulation, concedes less personal discretion to the auditor. The duty to disclose irregularities has not only been retained but has been extended to liquidators of co-operative societies.

The 2001 Act requires an auditor to certify that the society has complied with the provisions of this Act, and specifically *"whether the society has functioned in accordance with its Statute and the provisions of this Act"*.[51] The law is looking for an audit exercise which is more than a verification of numbers and figures. This new requirement should not be misunderstood to mean that the auditor is expected to police and monitor the society's daily acts and omissions. One would suggest that the law requires an auditor not to ignore troubling signals he may come across, even accidentally, during his engagement. An auditor should now be prepared to react appropriately whenever problems of a material or regulatory nature result during the course of an audit.

On the other hand, it appears unrealistic to interpret the law as requiring the auditor to undertake a separate speculative compliance-policing investigation parallel to the regular audit. The law does however imply that an auditor should be fairly knowledgeable of the provisions of the Act. It also expects him not to look the other way when evidence of corporate fraud or other material wrong-doing is unearthed.

The Co-operatives Board

Fundamental to the regulatory structure of the 1978 Act was the creation of a new licensing and supervisory public authority known as the Co-operatives Board. The Act assigned the Board extensive powers and functions intended to enable it to play the central role in the supervision, performance, conduct and promotion of the co-operative movement, and in the general administration of the Act. Indeed, the extensive role and considerable powers of intervention assigned to the Board probably constituted the most extraordinary feature of the now repealed Act. These powers were unduly intrusive and went beyond what a normal regulatory agency would need to exercise its functions effectively. While seeking to rectify this situation, the 2001 Act has nonetheless retained and confirmed the central role of the Board but has made a less intrusive instrument. It has chipped away at several powers no longer considered justified or necessary.

The 2001 revisions in this area respond to the need to re-adjust the focus of the Board's role in the new legislative framework, emphasizing its regulatory agency function. The changes introduced in the 2002 Act have helped to better re-define its core functions now reduced to their essentials. The Co-operatives Board still however maintains and exercises considerable supervisory authority.

While it is operationally independent, the Board falls under the political umbrella of the Minister responsible for Social Policy,[52] on whom it relies for appointment, funding and general political support.[53] The Board may only receive written general directions of policy from the Minister who may not intervene in decisions affecting the operations of particular co-operatives. The Board is obliged to furnish the Minister with all available relevant information to enable him to exercise his now reduced powers.

Although the Co-operatives Board is constituted primarily as a regulatory authority, it also acts as a registrar, the keeper and custodian of a publicly accessible registry, designated the Registry of Co-operative Societies. This registry contains important statutory and other documents pertaining to all registered societies.[54] The Board is both regulator and registrar.

It would be a misreading of the Act to suggest that the Board is now only comparable to the Registry of Companies under the Companies Act. The Board plays a more complex role as its supervisory and promotional functions have survived and indeed remain extensive. The Board may be described as playing these three fundamental roles, in order of importance: regulator, registrar and facilitator.[55]

As a registrar, the Board has responsibilities similar to other registrars. As a regulatory agency, the Board has powers similar to other regulators. Indeed, the extraordinary reserve powers now assigned to the Board to suspend a society's activities and replace the committee of management, where grave circumstances so warrant, have already been noted earlier. These powers are necessary to preserve the integrity of the co-operative sector, guarantee a degree of transparency and to prevent abuse of the co-operative form. The new Act safeguards and upgrades the Board's powers of enquiry and investigation and adds new powers to impose fines on uncooperative societies and their officials for contravening the Act. While removing certain functions envisaged in the 1978 Act, the new law has strengthened the Board's enforcement powers, making it into a more effective agency.

Indeed, a new provision in the 2001 Act gives authority to the Co-operatives Board to impose administrative penalties.[56] No similar power existed under the 1978 Act and its introduction was meant to encourage more compliance with the law's requirements. It is not meant as a revenue-collecting measure but rather as an effective deterrent to enable the Board to impose a degree of order in the area under its statutory jurisdiction. It is a normal power assigned to regulatory authorities. Additional ministerial regulations were issued in 2003.[57]

Under the new Act, monetary fines may be imposed on a co-operative society, its officers and its auditors. In each case, the penalty may be imposed for a breach of the Act or of an order issued by the Board. The law sets out the procedure to be followed when the imposition of a penalty is being contemplated. This serves to protect the due process rights of the person or society being accused of the breach.

One may describe the primary functions of the Board as follows:

- to promote the co-operative movement in Malta;
- to assist and facilitate the formation of co-operatives;
- to receive and process applications and to register new co-operatives;
- to supply information on co-operative societies;
- to monitor and supervise the general performance of cooperatives;
- to oversee the administration of the Act
- to ensure compliance with its provisions.

The recent amendments have made the Board's position more coherent, permitting it to concentrate its attention and to employ its scarce resources on leaner and more precise core functions.

To conclude this part, what follows is a non-exhaustive list of functions and powers assigned to the Board by the 1978 Act and which the 2001 Act has either eliminated or reduced. This list should better illustrate the backdrop to the recent reforms in the role of the Board and the motivation behind the changes.

(a) It was expected to act as advisor to government on co-operative matters, including *financial assistance.*[58]
(b) It was expected to *exercise control* over co-operatives.[59]
(c) It was expected to *encourage the establishment of co-operatives* and *to help them to increase their efficiency.*[60]
(d) It was obliged to provide the services of specialised personal to assist in the *formation, organisation and operation* of co-operatives.[61]
(e) It was obliged to provide *technical advice to all kinds of societies registered under this Act.*[62]
(f) It was expected to disseminate information regarding *co-operative principles, practices and management….*[63]
(g) It was obliged to assist officials of a co-operative *in complying with the provisions of this Act and in achieving the objects and purposes of the society on a co-operative basis.*[64]
(h) It approved the appointment of the auditors of each single co-operative as well as their professional fees.[65]
(i) It was obliged to *supervise the auditing of every society.*[66]
(j) It had the right to *attend general meetings and committee meetings of any co-operative* and to request copies of any relative agenda, notice, minutes and relative correspondence.[67]
(k) It had the right *to convene a special general meeting* of a society and determine the agenda.[68]
(l) It could appoint *one special member* on the committee of management and one on the supervisory board

of a co-operative which had received government financing.[69]

(m) It approved loans by one co-operative to another and determined the maximum amount that a cooperative could borrow.[70]

(n) It approved and imposed conditions on any proposed issue of bonds or debentures by a society.[71]

(o) It had to review for approval certain investments of funds by co-operatives.[72]

(p) It had the authority to direct a co-operative to rectify any *defects disclosed in the audit, inquiry or examination of its books*.[73]

(q) It could be requested to hear and to determine (or refer to arbitration) disputes that may arise between a society and its members or officers, between members of the same cooperative, between different cooperatives; it could change its mind on the approach initially adopted thereon, but in any case its decision was *final*.[74]

(r) It had to determine and decide any dispute on the interpretation of a society's statute and its ruling was *final*.[75]

(s) It could prescribe what books and accounts a co-operative shall keep and what returns were to be submitted to the Board.[76]

A Note on the Central Co-operative Fund

For a company lawyer, one of the more surprising features introduced in the 1978 Act and retained in the 2001 Act is the constitution of the Central Co-operative Fund. This fund is a typical feature in co-operative legislation, but would be simply unheard of in any other commercial or company law context. This Fund is often described as enshrining the solidarity objective which the Act seeks to promote as an essential and vital feature of co-operative activity. In order to avoid unnecessary misconceptions, it may be explained at the outset that this fund is not a tax or other fiscal imposition.[77] It is not a fund to which all registered co-operatives are obliged to contribute some annual fee, sum or percentage of turnover. Nor is it a variation of the compensation funds established under local and EU financial services rules and which are intended as a safety-net for investors.[78] It is actually a unique and simpler concept. Those co-operatives whose annual audited financial statements show a surplus contribute to the Fund to the extent of five per cent of such surplus. Consequently, only profitable societies fork out their five per cent, whereas those whose accounts disclose an absence of a surplus do not.

The Fund is established for specific purposes linked to the notion of solidarity between co-operatives. The objectives of the Fund echo the Co-operative Principles already discussed earlier. Article 86 of the 1978 Act had described these objectives as the "*furtherance of cooperative education, training, research, audit and for the general development of the co-operative movement in Malta*".

The equivalent article in the 2001 Act is article 91 which has refined the original rule and is now much more detailed and comprehensive. It has clarified that the five per cent contribution is calculated on the basis of all sources of an eligible co-operative's income, including income from investments. For the first time, the Fund has been vested with separate legal personality. It is now specifically assigned responsibility for collecting sums due to it by societies eligible to contribute the five per cent of surplus. These provisions have resolved problems that had been encountered under the less detailed 1978 framework.

The Central Co-operative Fund Regulations[79] issued by the Minister complete the framework for the proper administration of the Fund. They establish a joint committee made up of two members nominated by the Board and four representatives of registered co-operatives. The Apex nominates one other member. This committee is obliged to *"exercise a high degree of diligence in administering the funds under its responsibility"*. The Regulations require the keeping of proper accounts and records of all the financial transactions of the Fund as well as an annual audit. Regulation 3 sets out in some detail the purposes for which the Fund's assets may be employed. Emphasis is placed on education, training and research on co-operative activity.

The Co-operative Societies Act 2001 and Company Law

The context

The Co-operative Societies Act of 1978 contained 117 articles and two schedules. Adopted by Parliament after a lengthy debate, this Act may be considered the first modern local law to regulate co-operatives. It was repealed and replaced in 2002 when the 2001 Act came into force.

The Commercial Partnerships Ordinance,[80] consisted of 195 articles and four schedules. It entered into force in 1965. The Ordinance may be considered the first modern company legislation in Malta. The Commercial Partnerships Ordinance was to limited liability companies what the 1978 Act had been to co-operatives. The Ordinance remained in force until 1996 when it was replaced by the more voluminous Companies Act of 1995 with its 431 articles and eleven schedules.

Slightly less than 120 co-operative societies have been set up and registered since 1947. At the time of writing,[81] about sixty co-operatives remain on the official register. A few of these may be barely operative. On the other hand, almost 38,000 private limited liability companies have been registered since 1965, of which about 22,000 are operative. It may be broadly stated that the 2001 Act is to the 1978 Act what the Companies Act of 1995 is to the 1962 Ordinance; not a radical departure or complete break with the past, but a further development and maturity of ideas and mechanisms based on the former foundations.

It would probably have been easier to compare the 1978 Act to the 1962 Ordinance. In 1978, both sectors and their respective legislation were in a somewhat similar or comparable stage of development. Even the laws were more or less of equal length and detail. The Companies Act 1995 appears to be in a league of its own; it is much more detailed, sophisticated and complex. After all, the 1995 Act deals with the most important business form in local practice. Its provisions reflect the very flexible nature, economic significance and needs of the company model which it regulates.

There is no intention here to imply that the 2001 Act is not itself a complex and sophisticated law which has responded well to the modern needs of the sector it supports and regulates. It may also be worthwhile noting that whereas the Companies Act was to a relevant degree inspired by and based on the UK Companies Acts, the new Co-operative Societies Act is almost entirely home-grown.

Article 117 of the 1978 Act

The very last article of the Co-operative Societies Act 1978, article 117, was a most puzzling section and in fact has not been retained in the 2001 Act. This article stated that the provisions of the Commercial Partnerships Ordinance, or any enactment replacing it, do not apply to co-operative societies. It is not obvious why it was felt necessary to insert this provision in the first place, because Maltese law never said or implied that company law rules applied to co-operatives. The article possibly disclosed a lingering fear by its drafters that should the 1978 Act be found wanting or unclear in any respect, the relevant provision of the Ordinance would have been applied to co-operatives. The legislator evidently felt that this hypothesis had to be explicitly excluded.

The exclusion of company law as a possible reference point for co-operatives is perhaps broadly understandable. By and large, company law is more "capitalist" and profit oriented, tending to emphasise values incompatible with pure co-operative ideology. In company administration practice, one traces a bias towards individual personal property, profits and dividends, the acquisition of shares and the accumulation of voting rights and controlling powers. Company law has less regard for more generalised or collective interests, for solidarity among members and among the corporate entities themselves. These differences were deemed sufficient to make company legislation unsuitable as a possible point of reference for co-operatives law. Article 117 disclosed a certain allergy to company law.

Co-operatives are different

For both practical and academic reasons, a comparison between co-operative law and company legislation should prove interesting and educational. As a form of business organization, the co-operative offers an alternative to the limited liability company.[82] The question is whether the co-operative model has what it takes to offer itself as a truly credible and workable commercial alternative, in all instances.

Similarities

It would be simplistic and unduly bold to base important conclusions on a mere comparison between the individual articles of the 2001 Act and the provisions of the Companies Act 1995. But lists are often a useful exercise nonetheless.

Companies and co-operatives differ in many respects, concerning their social objectives, their structure and in the motivation underlying their regulation. Yet they clearly share several features. Even where common concepts or mechanisms are shared, the details may be quite different. The following is a tentative indication of the common ground:

(a) both constitute a form of business organization set up by persons who wish to associate to pursue some economic or other venture together;
(b) both forms of organization have been given a separate identity, a legal personality distinct from that of its members;
(c) incorporation is obtained by registration by a pubic agency and the fact is recorded in a publicly accessible registry;
(d) legal personality continues even during the winding-up and ceases upon being struck off the official register;
(e) the limited liability of the members is safeguarded;
(f) the committee of management mirrors the board of directors;
(g) both are obliged to keep proper books of accounts;
(h) both are obliged to appoint an auditor and to have their accounts audited;

(i) they share the concept of a "dividend", which is similar though not identical;
(j) the members' general meeting is the highest organ;
(k) both are required to maintain a register of members;
(l) the co-operative statute mirrors the Memorandum and Articles, and both share the trend towards document standardization;
(m) they share similar concerns relating to good corporate governance;
(n) the basic procedure for dissolution and winding up is similar, although the Board plays a more intrusive role than the Registrar;
(o) the possibility of investigations or enquiries by the Registrar applies also in the co-operative framework;
(p) the respective laws allow corporate reconstructions by way of mergers and conversions;
(q) in some countries co-operatives are regulated as a category of company law understood in a broader sense than is found in Maltese and UK law;
(r) at the European level, the *Societas Europaea* mirrors the concept of the *Societas Europaea Cooperativa*.

Differences

This part shall attempt to bring into sharper relief the difference between a co-operative society and a company by concentrating on concepts, structures and other features found in the co-operatives legislation with no parallel or equivalent in company law. This list of differences is illustrative rather than complete:

(a) Co-operative laws foresees a regulatory authority with extensive supervisory and powers of intervention and enquiry. The Co-operatives Board has wider and more varied regulatory powers of intervention than the Registrar of Companies.

(b) A co-operative requires a licence from the Board. The Registrar has no licensing power.

(c) The Board at its discretion (exercised reasonably) determines whether or not to register an applicant society. It examines the promoters' proposals and business plans. Company registration is more or less automatic once the formal documentation is correct, and the Registrar has no discretion to refuse applications except for submission of incomplete documentation. In practical terms, it is much swifter and easier to set up a company.

(d) Unlike co-operatives, companies do not undergo or enjoy the possibility of provisional registration, (though historically this was not always the case).[83]

(e) Co-operative promoters are obliged to appoint a formation committee to draw up a feasibility study, assess membership, and organize educational meetings.

(f) Co-operative law shows a marked preference towards individuals as members and establishes restrictions on corporate members.

(g) The duty of co-operatives to adhere to defined cooperative principles finds no parallel in company law. No set of principles or values govern the setting up of companies or the conduct of their controllers. Co-operative law stresses the principles of pursuing common interests, solidarity and one member/one vote, irrespective of shares held. The declaration of principles is one of the most remarkable distinguishing features.

(h) Co-operatives enjoy the choice of establishing a second-tier oversight supervisory board. Maltese company law only recognizes the board of directors, irrespective of the company's size or number of employees.

(i) The specific positive duty imposed on the auditor to notify the Board of any irregularities is not found in Company law.

(j) Nothing similar to the concept and functions of the Apex organisation and the Central Co-operative Fund are found in company law.

(k) The notion of patronage refund is unknown to company law.

(l) The Board's consent is required for the dissolution of a co-operative, in most cases. The Registrar's consent is never required for company dissolutions.

(m) The Board enjoys extensive powers concerning the appointment and supervision of a liquidator. No similar powers are assigned to the Registrar.

(n) Company law contains nothing similar to the notion of the Co-operative Societies Liquidation Account.

(o) Co-operatives have to satisfy certain conditions when seeking to establish subsidiary companies. Companies do not face similar restrictions.

(p) Co-operatives are not required to pay any fees to the Board other than a nominal initial registration fee.[84] On the other hand, companies pay substantial registration, annual and other fees to the Registrar.

Another potentially important distinction arises from Maltese fiscal legislation. Unlike companies, all co-operatives (and the Central Co-operative Fund) have been exempted from the payment of income tax. This may place co-operatives at some advantage over companies. The exemptions were issued under the Income Tax Act 1948[85] and not under the Co-operative Societies Act.

Companies are different

For the sake of completeness, one may now attempt a reverse exercise and point to a number of concepts and possibilities found in the Companies Act, not reflected in co-operative legislation. These are but some of them:

- (a) A private company may be set up as single member company; a co-operative requires at least five members.
- (b) Company law recognises three different types of commercial partnerships having distinct liability implications.
- (c) Company law allows a variety of structures, from the private company to the public company and the SICAV.
- (d) Various forms of winding-up procedures, reconstruction and special recovery proceedings are available for companies which are insolvent or in financial distress. The co-operative law approach is to rely on the intervention and supervision of liquidations by the Board.
- (e) Company law contains different and more detailed rules on divisions and mergers.
- (f) The status and obligations of oversea companies are also dealt with in the Companies Act, as in the Ordinance before it. No such provision is made in the Co-operatives Societies Act.

The private limited liability company has proved by far to be the most popular form of carrying out business in Malta. Company registrations continue at a steadier pace. Companies are of course much more loosely regulated and may be set up much faster than co-operatives which are still obliged to follow a rather cumbersome formation procedure. Nonetheless, it is suggested that co-operatives fill a void which companies might not always adequately satisfy. Particularly where promoters are seeking to carry on a joint enterprise with a structure promising a more integrated relationship between the members based on principles of equality and solidarity.

The more popular limited liability company model has overshadowed the co-operative in Maltese commercial practice, public perception and academic interest. Very clear similarities exist between a co-operative and a company and they share several common elements. However, sufficient differences allow them to remain conceptually and functionally distinct. The new Co-operative Societies Act 2001 has stressed, not reduced, these differences.

A judicious transposition to the co-operative model of some of the strengths and advantages of the private limited company should prove beneficial provided the exercise safeguards the special identity of the co-operative model and respects its history and distinct social function.[86]

A Note on the International Dimension

Cooperatives are not just a national phenomenon but have a highly developed international context with the involvement of huge international entities as the United Nations (UN),[87] the International Labour Organization (ILO)[88] and the International Cooperative Alliance (ICA).[89] The new Co-operative Societies Act has for the first time introduced an indirect link to the international dimension. We have already seen that this has been achieved by the adoption of a set of co-operative principles promoted by the ICA

The 2001 Act is silent on another important aspect of the international context, the European Union. The new Act was passed prior to EU membership which came three years later. It is not really within the scope of this paper to analyse EU law in this area. For the sake of completeness and to place the new Act within Malta's new EU obligations, a brief reference shall now be made to some relevant legislative developments.[90]

The first measure is ***Council Regulation (EC) No. 1435/2003 of 22nd July 2003 on the Statute for a European Cooperative Society (SCE).***[91] Being a Regulation, this measure has direct effect in the legislation of member states and requires no transposition measure. The model adopted follows closely the European Company Statute[92] model adopted by the EU some time earlier. The objective is simply to have a co-operative society recognized and able to operate in all member countries despite being incorporated in one member state. Differences in national rules in the Union on co-operative societies are considerable. In some countries co-operatives are regulated as an integral part of company law. Denmark which boasts of a significant co-operative movement belongs to a group of countries which have no special law on co-operative societies, but regulate them under general law. Italy and others deals with co-operative societies at least partially through its Civil Code. As we have seen Malta has a special law dedicated to co-operatives, distinct from both the Civil Code and the Companies Act.

The Council Regulation does not seek to super-impose a European model on all member states. Member states in fact retain competence over national laws regulating co-operatives. The rules on the European co-operative are intended to co-exist with the diverse national law rules on the setting up and regulation of co-operative societies.[93] Recital number 6 of the Regulation refers to the Resolution of the 88th Plenary of the General Assembly of the United Nations of the 19 December 2001 (A/Res/56/114). This

Resolution *"encouraged all governments to ensure a supportive environment in which cooperatives can participate on an equal footing with other forms of enterprise"*.[94]

A second EU measure is a directive - ***Council Directive 2003/72/EC of 22nd July 2003 supplementing the Statute for a European Cooperative with regard to the involvement of employees.*** This directive governs employee participation in co-operative societies. It sets out their rights to information and consultation. This too is modelled on a similar earlier directive applicable to companies.

Finally, the international dimension is now acknowledged in the 2002 regulations governing the Central Co-operative Fund, discussed earlier in this paper. Fund assets may now be allocated *"to support and intensify the participation of the Maltese co-operative movement in relevant organizations, activities and projects on an international level"*.[95]

An Assessment, a Conclusion and the Future

Inevitably, the co-operative form always finds itself compared to the limited liability company, and co-operative law continues to be compared to company law. Indeed, the Board policy document approved in October 1993 had highlighted the need to project co-operatives as *"an attractive legal alternative to the conventional limited liability company and partnerships"* and as *"attractive to other professional advisers who may recommend cooperative options to clients"*.[96] Will the co-operative form manage to extricate itself from the long shadow cast by the more popular company model?

Like most other areas of law, co-operatives legislation needs to evolve, absorb new concepts and to have an opportunity to refresh itself periodically. In this way, it may keep up with changing requirements of societies, members and major changes in public expectations and perceptions, local and foreign. This process should ensure that the co-operative model remains dynamic, attractive and competitive. The 2001 reform may be best viewed in this context.

There seems to be a broad consensus in Malta in favour of the proposition that co-operatives should be regulated by a special law. This culture still favours a public law approach through the establishment of a government-appointed and funded supervisory agency also doubling as registrar and serving as an intermediary between the operators and the state. It seems highly unlikely that strong support would be found for a suggestion that co-operatives should simply be regulated by the ordinary rules of law or that the Co-operatives Board should be done away with.

Was the 1978 Act a success? This Act offered a relatively neat and user-friendly framework that allowed co-operatives in Malta to flourish while being subject to firm and fair regulation. Although a product of its time,[97] the Act was a worthy measure and merits a broadly positive assessment. The 1978 Act is now consigned to history, but it still deserves academic attention. The 1978 law largely achieved its objectives and served the co-operative movement well.

The 2001 Act has followed quite closely the basic structure of the 1978 Act. This ensured continuity and avoided uncertainties and disruptions in the sector, especially during the change-over period. The new Act is however very different in many respects. A number of changes relate to substantial issues, others to detail; some are very evident while others are less obtrusive. It would certainly be a mistake to under-estimate the conceptual and practical relevance of the divergences. Few, if any, of the provisions of the 1978 Act remained unaffected by the 2001 reforms.

A somewhat similar process occurred in the company law field. By the early 1990's, much of the 1962 Ordinance had become out-dated and inadequate. It was eventually replaced in its entirety by the 1995 Act, a step that had been long overdue.

The 2001 Act also appears more outward-looking in its approach. It has considerably widened the scope for the establishment of new co-operatives and new corporate arrangements under which they may prosper. Co-operatives may have themselves partly to blame if bad press influences public perceptions about them.[98] Co-operatives need to properly exploit the more flexible opportunities and innovations offered by the new law, and, in a way, re-invent themselves. If this occasion is missed, public perception that co-operatives are frozen in time may be strengthened.

Will the 2001 Act prove a success? It is still too early to make a serious and objective assessment. This Act has sought to make Maltese co-operative law neater and more precise, removing some archaic rules and restrictions, and creating a more supportive and flexible framework for the further development and expansion of co-operative societies into wider areas of activity.

The 2001 reforms were a necessary step in the evolution of co-operative regulation in Malta. The new law is a more modern instrument permitting co-operatives to better compete with other business organizations in the private sector, and to respond efficiently to the tremendous changes that have occurred since 1979 in the local and global social, economic, technological, legal and political fields, and in public expectations. However, as in any other regulated sector, the law can at most provide a workable and supportive environment; it cannot also guarantee the commercial success and profitability of co-operatives.

Selected publications and materials

1. Baldacchino, G., 'Human Privatization: Worker Co-operatives Initiatives in the Public Sector', Journal of Co-operative Studies, Vol 31, no 1, May 1998;
2. Baldacchino, G., 'Cleansing the Co-operative', The Malta Independent on Sunday, 6 June 1999;
3. Baldacchino, G., Fabri, D., Micallef Attard, R., papers presented to an Information Seminar organized by the Co-operatives Board on 'The Co-operative Societies Act: New Responsibilities; new Possibilities', 29 May 2003;
4. Co-operatives Board, Proposed Policy for the Development of Cooperatives in Malta, November 1993;
5. Co-operatives Board, Directory of Co-operatives;
6. 'Koperattivi' (formerly called 'Il-Fuljett tal-Koperattivi'), a quarterly newsletter sponsored by the Central Co-operative Fund;
7. Munkner, Hans-H., 'Report on the Promotion of the Co-operative Movement in Malta', prepared for the German Agency for Technical Cooperation Ltd, Marburg, April 1980. This comprehensive report is essential reading and deserves to be better-known. It provides extensive background to the drafting of the 1978 Act. An earlier version of this report, prepared in March 1976, laid the foundations for that Act and to the repeal of the 1946 Ordinance;
8. Munkner, Hans-H., 'Development Trends of Co-operative Legislation in European Union Member States', University of Marburg, 2000;
9. Munkner, Hans-H., 'Co-operative Principles and Values – Developing Co-operative Societies in a Globalised

Economy', Malta Co-operative Day address, 5 July, 2003;
10. Parnell, E., 'Re-inventing co-operation: the challenge of the 21st Century', Plunkett Foundation, Oxford, UK, 1999 (formerly published as 'Re-inventing the co-operative – Enterprises for the 21st Century', 1995);
11. 'Report of the Commercial Partnerships Law Reform Commission accompanying a draft Commercial Partnerships Bill', Department of Information, February 1956;
12. 'Report of the Ministerial Committee on the Development of Economic Democracy in Malta', Malta University Print, 1993;
13. Shah, A., 'Cooperative law: An instrument for development?', International Labour Review, Vol. 131, 1992.

Related publications and materials by the author

1. Fabri, D., 'The Companies Bill', address to a public seminar organized by the Institute of Directors, 7 December 2004;
2. Fabri, D., 'The new Co-operative Societies Act 2001 – a case of new wine in old bottles?', The Sunday Times, 14 April, 2002;
3. Fabri, D., 'The Law regulating Co-operatives and the Auditor', The Accountant, September 1999;
4. Fabri, D., 'Forms of Business Organizations and the role of the MFSC', address to seminar on "Increase your efficiency through knowledge", jointly organized by Bank of Valletta plc and the Ministry for the Self-Employed, 6 June 1998;

5. Fabri, D., 'The Historical Background: need for review of the legislation; overview of changes', address to the Seminar on the new Companies Act, organized jointly by the Malta Institute of Accountants and the Chamber of Advocates, 13 November 1995;
6. Fabri, D., 'The Evolving Role of the Registrar', address to the Seminar on the new Companies Act, jointly organized by the Malta Institute of Accountants and the Chamber of Advocates, 17 November 1995.

Some Useful Websites

1. www.coopsboard.org
2. www.ccf.org.mt
3. www.scoops.org.mt
4. www.msp.gov.mt
5. www.education.gov.mt/employment/coops/archives/coops
6. www.ica.coop
7. www.copacgva.org
8. www.fao.org.documents
9. www.ilo.org
10. www.mcba.coop/chisa
11. www.australia.coop
12. www.coopscanada.coo
13. www.co-opstudies.org
14. www.coopdevelopment.org.au
15. www.plunket.co.uk
16. www.usaid.gov

Notes

1 The document had been approved by the Board at its sitting of the 12 October 1993. Several of the proposals contained in this publication have been implemented in the 2001 Act.
2 The Times, 6 July 1996.
3 On the 26 February 1999, The Times opened its unusually enthusiastic editorial with the flowery remark that *"Few things could ring more pleasantly upon the ear than the news that in the coming months the government plans to amend the law regulating co-operatives in order to encourage the formation of new ones*." The editorial ended on an equally optimistic tone: *"If the board is seen as an enabler rather than a paternalistic regulator of every little detail, it will be the economic catalyst it is intended to be*.".
4 The entire drafting exercise was driven all the way to fruition by the Board in conjunction with the strong political support of the then Minister for Social Policy, as well as in consultation, though not necessarily always in agreement, with the Apex representatives. The main drafters were the then Chairman, Prof G Baldacchino, who has written extensively on co-operative issues, and the writer, who served as Acting-Chairman of the Board.
5 See Dr Walter Cuschieri et vs Onor Prim Ministru, Constitutional Court, 30 November 1977.
6 Article 21 of the Constitution.
7 Chapter 386 of the Laws of Malta.
8. Article 3(3) of the 2001 Act.
9 Article 3(1)(c) of the 1978 Act.
10 Article 1(2) of the 2001 Act.
11 The entire Act was not brought into force at one go. Most provisions came into force on 16 April 2002, but thirteen provisions were delayed until 1 July 2002. This measure allowed registered societies sufficient time to implement the necessary adjustments to their statutes.
12 Article 111 (1) of the 2001 Act.
13 Article 111 (2) which safeguards the validity of *"any registration, authorization, approval, appointment, order, regulations or other action whatsoever made and issues by virtue of the repealed Act*".
14 Soon after the new law was passed in 2001, the Board sent a circular on the subject to all co-operative societies on its register advising them of their need to review their statutes to bring them in line with the new Act.
15 See the ICA website for more useful information on co-operative principles and legislative policies and developments globally.
16 See the original formulation in article 21 of the Constitution. The improved formulation now found in article 21 (3) of the 2001 Act was initially developed in article 43 of the Consumer Affairs Act 1994, Chapter 378 of the Laws of Malta. This Act set out for the first time in Maltese law a declaration of "Consumer Rights", a context comparable to the declaration of co-operative principles.
17 Chapter 379 of the Laws of Malta.
18 The island became a member of the EU in May 2004.
19 Clearly, no similar provision could have been found in the 1978 Act

enacted sixteen years before Malta adopted its first ever law to regulate competition.

20 See articles 66 (4) and 45 (4) of the 1978 Act.

21 Remarkably, voluntary associations are still not subject to any special law in Malta. This constitutes a serious lacuna which however may be rectified in the near future following the publication of a White Paper "Strengthening the Voluntary Sector" in July 2005 by the Ministry for the Family and Social Solidarity. The White Paper included a draft bill which envisages the comprehensive regulation and supervision of associations and several other unregulated entities, and the appointment of a Commissioner for Voluntary Organizations. The documents may be accessed at www.mfss.gov.mt .

22 It is interesting to note that the original version of these two provisions formed part of the 1946 Ordinance. This had allowed an appeal in both instances to no less than the Governor himself. See articles 7 and 9 of the 1946 Ordinance.

23 Article 4.

24 See new articles 36 and 109.

25 Established by Part II of the Arbitration Act, 1996, Chapter 387 of the Laws of Malta.

26 The Malta Business Weekly of 1-7 August 1996 under the heading *The Courts or the Co-operatives Board?* reported a decision taken on 11 July 1996 by the First Hall of the Civil Court in a case instituted by Ghaqda Koperativa tas-Sajd Limited (a fishing co-operative) against one of its members, C. Gafa. The court accepted defendant's plea that it had no jurisdiction in the case as disputes between a society and a member were reserved by the 1978 Act for decision by the Board. Interestingly , the court quoted from the relative Parliamentary debates during which the Minister piloting the then 1978 Bill had stated (in translation) : "*We want as far as possible to remove such issues from the Law Courts and channel them to the Co-operatives Board, that is the special board established to decide upon such matters…*". The judgement was confirmed in later cases, including Ghaqda Koperativa tas-Sajd Limited – vs – Tony Carabott where the same court, differently presided over, too lightly (and in the writer's view, erroneously,) considered the Board a "*special tribunal*".

27 Article 26.

28 See article 5 of the Ordinance.

29 In line with the 12th EU Company Law Directive, 89/667/EEC, a private company may now be set up as a single member company. See article 212 of the Companies Act.

30 Article 2 provides a definition of *subsidiary company*.

31 See *inter alia "First government cooperative set up*", The Times, 3 September 1996; "*Public sector cooperatives scheme under review*", The Times, Business, 14 January 1999; and *Public Sector coops: the best of both worlds*", G Baldacchino, The Malta Independent on Sunday, 19 May 1996.

32 Ordinary co-operatives cannot now exceed eighteen months under provisional registration. The rules on the provisional registration of societies were not substantially revised in the 2001 Act. Compare article19 of the 1978 Act to article 28 of the 2001 Act.

33 Article 71.
34 Article 78.
35 ibid.
36 ibid.
37 ibid.
38 Article 45.
39 See articles 67 and 69 of the 1978 Act.
40 Until rectified in 2003, a statement on the general duties of company directors was surprisingly and conspicuously absent from local regulation of company directors. The Companies Act was amended in 2003 (Act IV of 2003) for this purpose and a general statement has been inserted as article 136A.
41 Articles 83 – 85.
42 Article 85 (1).
43 Article 85(2).
44 New article 62 is equivalent to former article 55.
45 Article 66 (g) and (h).
46 Article 48.
47 Report of the Registrar of Co-operatives Societies for the year 1947-48, Department of Co-operatives, Valletta, 14 January 1949.
48 Article 39.
49 Article 18.
50 Article 31.
51 Article 49(4)(d).
52 Currently designated the Minister for the Family and Social Solidarity.
53 The Board consists of a chairman and up to six other members, qualified in terms of article 4, and appointed by the Minister responsible for cooperatives. See article 4.
54 This registry is now open to the public. See article 12. Regulations establishing fees for public inspection and for the production of copies were published in 2003 – (Legal Notice 198 of 2003).
55 Its latter role as promoter of the co-operative movement, though not entirely written off, has been somewhat reduced and, in practice, this role is now primarily undertaken by the Apex organization.
56 Article 17.
57 Co-operatives Societies (Establishment of Administrative Penalties and Sanctions) Regulations, 2003 – (Legal Notice 115 of 2003).
58 Article 3(1).
59 ibid.
60 ibid.
61 Article 94(1).
62 ibid.
63 Article 10(1).
64 Article 10(2).
65 Article 39(1) and 43.
66 Article 96(1).
67 Article 111(d).
68 Article 60 (4).
69 Article 79.

70 Articles 81 (1) and 82 (3).
71 Article 80 (3).
72 Article 83.
73 Article 99(2).
74 Article 109.
75 Article 27 (3).
76 Article 111 (a) and (b).
77 Unfortunately, co-operatives eligible to contribute to the Fund often do so reluctantly. In one particular case, payment claimed by the Board in favour of the Fund was contested on technical grounds and delayed for several years until the issue was finally determined by recourse to arbitration. During the arbitration proceedings, the co-operative tried to argue that the 5% contribution to the Fund was just another tax imposition burdening the society. The award was given against the co-operative.
78 These include the investors and bank depositors compensation schemes fund by contributions made by licensed firms. Unpaid investors of an insolvent firm may claim at least partial recovery of their loss. See the Investor Compensation Scheme Regulations, 2003-(Legal Notice 368 of 2003), and the Depositor Compensation Scheme Regulations, 2003-(Legal Notice 369 of 2003).
79 Co-operative Societies (Central Co-operative Fund) Regulations, 2002 - (Legal Notice 108 of 2002).
80 Ordinance X of 1962.
81 February 2006.
82 In his provocative article *Cleansing the co-operative* in the Malta Independent on Sunday, 6 June 1999, Dr Baldacchino discusses five *myths* about co-operatives, including one reading *"**Co-ops are not that different from companies**."* He admits that: *"This is a tricky one….**"**.*
83 In an interesting lesson from the past, provisional registration is not unknown in the history of company law. The (UK) Joint Stock Companies Act 1844, (which also created the office of the Registrar of Companies), had introduced a rather cumbersome registration procedure, consisting of two stages, provisional and complete registration. *"A provisional registration for a few preliminary purposes was followed by a complete registration, and only when the latter was completed did the company acquire corporate status*." Palmer's Company Law, 24th Edition, vol 1, 1987 (C Schmitthoff - General Editor). The Joint Stock Companies Act 1856 removed this cumbersome procedure and *"made the formation of a company a simple and inexpensive process*." (Palmer ibid)
84 Co-operative Societies (Levying of Fees) Regulations, 2003 (Legal Notice 198 of 2003).
85 Chapter 123 of the Laws of Malta.
86 Prof H. Munkner has cautioned against the trend of treating co-operative members as customers or shareholders as this weakens co-operative societies rather than strengthen them. See Hans-H. Munkner, *Co-operative Principles and Values – Developing Co-operative Societies in a Globalised Economy*, Malta Co-operative Day address, 5 July, 2003.
87 See United Nations Guidelines on Cooperative Development 20010 elaborated in cooperation with COPAC.

88 International Labour Office Recommendation 193: "Promotion of Cooperatives". The ILO has a specialized branch which deals with cooperatives and cooperative law developments. A database of cooperative laws has been set up. Malta's 2001 law may be found there.

89 The ICA is an important part of the international cooperative movement network and a vital point of reference. Its useful website is accessible at www.coop.org. The national member for Malta is the Apex Organization of co-operatives. The ICA and the ILO collaborate closely. They signed a memorandum of understanding in February 2002.

90 See generally, Felice Pace J., Facing the challenges of globalisation; co-operative enterprise in an EU context, The Sunday Times, 2 March 2003, and "Is-Socjetà Koperattiva Ewropea qrib li ssir realta", Koperattivi, newsletter published by the Central Co-operatives Fund, April-June 2005.

91 The *Societas Cooperativa Europaea* (SCE).

92 The *Societas Europaea* (SE), Council Regulation (EC) No 2157/2001of 8th October 2001 on the Statute of the European company.

93 EUROPE news Bulletin, No. 8460, 13 May, 2003.

94 See also Report of the Secretary-General on the "Status and Role of co-operatives in the light of new economic and social trends" to the 44th session of the General Assembly on the 23rd December 1998. The Report provides an interesting discussion on co-operative legal structures and an overview of international developments and changes in co-operative law in various countries.

95 Regulation 3(1)(g).

96 No. 1 above.

97 A time of intensive state intervention and centralization, evidenced by wide ministerial powers.

98 Regrettably, co-operatives generally suffer negative public perceptions. Except for persons and professionals who work in the sector, co-operatives are broadly perceived as an unfashionable subject for discussion. They also tend to get a bad press. During the past few years co-operatives have frequently been in the news; often for the wrong reasons. Many reports have featured co-operatives in financial or operational difficulties. Numerous newspaper and television reports throughout the first two weeks of August 2002 and again in 2005 covered the serious problems faced by the Koperattiva Indafa Pubblika Limitata (KIP). See "Gonzi issues stern warning to cooperative", The Times, 16 July 2003. (See also report in The Times, 18 February 2005 on same problem.

E. P. DELIA

ECONOMIC EFFICIENCY, SOLIDARITY, AND THE CO-OPERATIVE MODEL: LESSONS FOR MALTESE CO-OPS

Two judicial protests submitted to the Commission for Fair Trading and the First Hall of the Civil Court claim that two Maltese co-operatives in the agricultural sector control their respective market to the detriment of business in general and their members in particular. The Commission for Fair Trading gave a ruling in 2000 to the effect that one co-operative was abusing its dominant position in the market for pasteurised milk in the Maltese Islands. This was happening at the expense of consumers and producers; it was forcing its members to act in ways that were not conducive to the sustainability of their business operations; and the co-op was administering funds that should instead be distributed to its members. (Commission for Fair Trading, 2000, Request No 1/99). A similar statement was made regarding the activities of another co-operative in the animal breeding sector: one producer claimed that this particular co-op was acting in direct competition with its members, while it enjoys total monopoly in the sector even after Malta's membership of the European Union, and was generating profits for the central fund from the sale of imported animals paid for by a state subvention. (*The Times*, Malta, 2005:15).

Similar claims are made at times for other world-renowned co-operatives. Mondragon Co-operative Corporation in the Basque region of Spain has been under observation in terms of its institutional evolution in the past decade. For example, Mondragon's rules specify that up to 70 per cent of profits should be added to owners' capital accounts, at least 20 per cent to reserves, at least 10 per cent to the community. There were times when these rules were not observed; in some years only about 20 per cent of net profits were added to owners' capital accounts while about 75 per cent were added to reserves. At the same time salary differentials were widened after an organisational restructuring in the early nineties. These changes tended to concentrate power in the hands of managers, pushing policy setting and control of management activities away from owners towards an upper level of senior executives. To that extent the accountability of managers to members (the co-op owners) were reduced. (Davidmann, 1996) In turn, the objective that managers aimed to achieve tended to veer towards profit maximisation in line with the acclaimed aim of the capitalist firm.

Indeed, in going global, through the Mondragon Co-operative Corporation (MCC), Mondragon adopted the traditional capitalist employer structure, at times in conjunction with capitalist partners, which companies do not seem intended to be eventually converted into co-ops. At the same time, co-ops engage non-members on the grounds that the global market requires a more dispensable sector of the workforce; up to 40% of employees may be non-members. It is argued that structural rigidities fossilize a firm's future development and lead to its decline. Therefore, the firm has to be flexible enough to anticipate change and respond fast to it.

Examples like these call for a re-assessment of the co-operative model in a globalised trade environment, and more specifically, in the context of the Single market of the European Union. There are various institutions that claim to belong to the 'co-operative class' but they differ in their proper objectives and in the means to attain such objectives, including their administrative set up. At a time when the EU is moving towards a harmonization of legislation that governs co-operatives, such a query is important. The euro zone did not perform economically as robust as other developed countries, such as the United States of America. So a close look at the relevance of institutions, including the legal form of economic organisations, may be conducive to a better understanding of the factors that can positively influence sustainable and stable economic growth over time.

This paper follows this query with emphasis on the role of co-ops in this transitional phase for the Maltese Islands. Co-ops have been operative in Malta on a relatively wide scale, but primarily in the agriculture sector, for the past sixty years. There are at present fifty-five registered co-ops, seventeen of which operate in the sector of agriculture and account for around ninety percent of total co-op turnover and membership. The co-op model was introduced in most economic sectors except retail trade and housing. It has found government support and co-ops relied for a long time on such government assistance; this included tax considerations, cash injections, staff secondment and import controls via seasonal quotas and tariffs. Legal notices created sheltered, monopolistic/ologopolistic market structures that were aimed to support herdsmen/farmers' income or to guarantee work for so-called workers' co-ops that were instituted to hive off employment from the public sector.

Given this fiscal backup, co-ops have been generally successful but, surely, not problem free. This 'artificial' set up did not permit them to evolve as other independent associations might have done in their quest for survival. In fact, Maltese co-ops in agriculture are judged lacking proper technical and marketing management; they failed to keep abreast with technological progress and automation; they suffered from lack of loyalty and support from their members; and they failed to make timely decisions to rectify such shortcomings (Walker, 2004). One may claim that they did not prepare themselves for Malta's membership of the European Union. They saw themselves more as pressure groups that expected government to obtain favourable terms of accession and integration, preferably sustaining the status quo, rather than as autonomous groups of like-minded people who anticipated change and prepared themselves to meet it head on!

Witness the collapse of Maltese co-ops in certain sectors of agribusiness activity and the public waste disposal sector, with the latter ending with a default of a main co-op (Public Cleansing Co-operative–KIP) that owed Lm950,000 in tax arrears and another Lm188,000 in social security contributions; a total amounting to Lm1.138million (2.65million euros). Add to this the ruling by the Commission for Fair Trading regarding fairness in trade and dealings within co-operatives and the importance of a critical analysis of the co-op model itself becomes evident.

This paper is developed in four stages. Part one examines the role of institutional development in the process of economic change. Part two identifies those conditions that lead to economic efficiency while part three focuses on the role of solidarity as a complementary objective that may support or thwart dynamic economic growth. The paper applies in turn the observations gained to the situation in the Maltese Islands, a time of reconsideration of the roles of the individual and the collective in a freer trade environment. Maltese producers have to abide by trade regimes that are not necessarily tailor-made to suit the particular demographic and geographical characteristics of the islands. It is a situation that calls institutions to respond in a context of uncertainty within a more competitive global trade regime and within freer labour and capital markets.

1. Institutional evolutions and the dynamic process of change

The merits of the co-operative model of organisation may be considered in terms of the role institutions play over time in the social and economic development of a region. In this context, the rationale may change as society and the economic environment in which it operates evolve. The merits of a co-operative may also be evaluated in relation to its contribution to personal fulfillment in the context of specified ethical goals. Personal and social values such as solidarity and wide participation in economic gains have to be considered in tandem with economic efficiency and sustainable long-term economic growth. In this context, efficiency and co-operation constitute one element in the wider debate on the role of production and a fair income distribution over time in a society.

There may be different forms of organisation that invoke simultaneously solidarity, democratic decision-making, co-ownership of assets and distribution of value added according to a pre-set pattern. Apart from co-operatives, workers' participation set up, employee stock option plans, and the 'economy of communion model' are three examples of such a joint-objective paradigm of industrial organisation. They belong to the 'employee ownership' category of enterprises. Such enterprises arose for various reasons: to encourage economic development, to keep labour peace with an incomes policy, to save sinking firms, to privatise government-owned enterprises, to prevent buyouts and closure of small firms, to spread ownership of wealth or encourage employee loyalty in tight labour markets, and to generate higher overall economic productivity through capital investment and/or individual employee efforts. The list is unending! (Yates, 2001)

The *workers' participation model* has been talked about for many years in Malta and was 'implemented' at the former Malta Drydocks Corporation. This 'experiment' has apparently lost its appeal in the Maltese world of work since no one seems interested in discussing the idea any more. This could be the phase of low interest in this industrial paradigm that has been observed in several countries. But up to some time ago, it was argued, "there is a near national consensus that workers' participation is an ideal worth striving for. Yet such wide agreement in public with (this) principle is not easily translated into practical policies of implementation. The principle is often stifled as a result of traditional prejudices, socio-economic divisions and conflicting interests, both real and imaginary. As participation is concerned with power sharing, it is essentially a political goal and, in Malta, politics is undoubtedly a divisive subject" (Zammit, editor, 1989: 1).

But it may be claimed that the experiment failed not because of 'political rivalry' but because of a simple economic explanation: workers in self-managed industries cannot be made interested in placing capital where it is most productive. Once efficiency, that is the least cost principle, is pushed aside, the independent survival of the firm is jeopardised. The real test of 'industrial democracy' – even when participation is restricted solely to managing the firm – comes when decisions are to be taken regarding investment and the capital-labour ratios to be operated in order to generate work at minimum costs and at a profit. Workers in a self-managed firm will find it very hard to vote for a restructuring process that will see many of them becoming unemployed. Efficiency will be sacrificed; such a firm can only survive if it is subsidised from taxpayers' funds or if consumers pay relatively higher prices to keep the inefficient firm in operation. The lesson that one draws from this social experiment is to focus on the continuous search for efficiency and any short term financial support or legal protection has to be considered as a time for intensive economic assessment and organisational restructuring.

Employee stock option plans (ESOPs) have been tried on a very limited scale in certain state owned enterprises, mainly in the financial sector. It cannot therefore be said that this industrial paradigm had much 'success' in the Maltese Islands. ESOPs are tax qualified benefit plans in which most or all of the assets are invested in the employer's stock. Like profit sharing an ESOP generally must include all full-time employees meeting certain age and service requirements. The company can finance the plan through cash contributions; debt the company pays; or share contributions. Employees receive their benefits when they leave the company.

A culture of ownership is common at companies with ESOPs, but it is not typical of other employee-owned companies, even though granting stock options has increased in various countries in the past decade. However, it is hard to communicate clearly what ownership means and to instill a sense of true ownership. Creating an ownership culture is a demanding and time-consuming process (Rosen, Case and Staubus, 2005)

The *Economy of Communion model* of organisation, proposed by the Focolare Movement, was launched in 1991 (Bruni, 1999). The model emphasises a culture of 'giving' rather than a culture of 'receiving', a mentality that might have been reinforced inadvertently through relatively generous welfare support systems in various countries. The model envisages a communion of production, that is the emergence of enterprises that care for producers, their suppliers and consumers. It is based on the ideas of shared growth: all involved in the production and distribution of a good or service benefit from economic growth, quality enhancement, cleaner environment and a fair tax regime. The economy of communion model upholds the efficiency of the market system, the drive towards wealth creation and the generation of profits. Profits are distributed according to set formula. A third goes to support the growth of the enterprise; another third is paid to those workers who are in need or allocated to generate new employment in the firm; and a third goes to finance the spreading of the vision of the Economy of Communion.

Apart from basing the model on the underlying solidarity principle, the paradigm's vision is forward looking. It foresees a global trade environment where the relocation of capital chasing low wages in search of profits could one day be difficult to attain. The non-profit firm will therefore assume greater importance especially in the services sector.

However, a counter-idea seems emerging and taking hold in some countries: non-profits are starting to pursue complementary profitable initiatives to render themselves sustainable. In the United States, for example, many philanthropic foundations and other funders have been urging nonprofits to become financially self-sufficient and have aggressively promoted earned income as a means to 'sustainability'. As a result, nonprofits feel compelled to launch earned-income ventures, if only to appear more disciplined, innovative and businesslike to their stakeholders (Foster and Bradach, 2005).

Quite expectedly, the economy of communion model, still innovative as an idea, has had as yet only a very restricted appeal in the Maltese Islands (Delia, 2002: 3-26; Delia, 2002a: 1 –15). The model was launched at a time of intellectual reconsideration of the role, structure and governance of several forms at law of production/service entities. It has to compete for attention with other established forms of ownership and organisation.

Co-operatives have to be regarded as one other legal structure that stands as alternative to the joint-stock company. The 'co-operative identity' emerges from a set of basic principles: free admission to the co-ops; democratic administration and democratic supervision; racial, political and religious neutrality; distribution of surpluses according to transactions (in the case of consumer co-operatives); payment of limited interest and capital; continuous education of members. Other basic tenets may be introduced; they reflect the times and places of adoption.

If co-ops are to survive economic change they have to be part of it and seen contributing to the well being of their members and society in general. Wishful thinking regarding the desirability of this organisational model will not sustain the evolution of the unit. It will, therefore, either prove to be a weak operative instrument and fold out its activity or it will transform itself in another form of economic organisation and survive in its new format. It will thus transfer the co-op mold into another 'economic cum solidarity' make up or give up the intra-unit solidarity completely.

The survival of particular forms of organisation has to start from an understanding of the role of institutions in the long-term sustainability of economic development. Social and economic development is the result of a dynamic process. Therefore institutions have to adapt, self-transform, in order to remain a positive factor contributing to a community's well being.

Economic development is a complex phenomenon. It is the outcome of a continuous interaction among geographical factors, institutions and policies. Human behaviour, as reflected in entrepreneurial acumen and the markets for labour and capital, is conditioned by the interplay of these three sets of elements. Such behaviour drives ahead personal development and a person's contribution to output.

Recent research on global economic growth seems to suggest that there appears to be a close correlation between institutional quality and international income differences where the perceived 'quality' of institutions is seen as a prime factor *determining* economic and social development. Without minimising the possibility of reverse causality between institutions and geography/economic policies, yet the relative importance of institutional development for a country's overall economic welfare is coming strikingly to the fore (International Monetary Fund, 2003:26-45; and International Monetary Fund, 2003a: 95-128).

Economic literature defines 'institutions' along a wide spectrum. At one end the term stands for the formal and informal constraints on political, economic and social interactions. They are seen as setting up an incentive structure that reduces uncertainty and promotes efficiency, thereby reducing transactions costs and freeing resources to production and exchange. Thus, an efficient judicial system will over time induce economic efficiency by enforcing property rights and the rule of law in the process internalising third-party effects, both positive and negative, thereby bringing about a change in the behaviour of agents over a wide range of economic activity. (Delia, 2002: 47-68).

Concurrently, a greater openness to trade, stronger competition and higher transparency in policy formation and corporate governance are conducive to institution strengthening and growth. Policies, therefore, have a bearing on institutional quality. For example, opening up markets may help to weaken vested interests and reduce rents derived from prevailing economic and institutional arrangements. A freer trade environment may lead to demand for institutions more suited to an increasingly varied and possibly risky range of transactions and exchange. But above all, there has to be a commitment to adapt the institutional network to enhanced competitive challenges. There has to be strong leadership in the key institutional reforms if improvements in sectoral and aggregate performance are to be sustained.

At the other end of the range, the concept of 'institutions' refers to the degree of autonomy of certain policy decision makers, regulatory frameworks and procedural devices. Such institutions influence economic performance by inducing a coherent and consistent combination of policy choices. Examples include central bank independence; balanced budget conditions or the fiscal stability pact of the European Union with its specific targets for public sector deficit/Gross Domestic Product ratio and national debt/Gross Domestic Product ratio; the existence and structure of international trade agreements; and rules governing the performance of the markets for goods and services, labour services and capital movements.

One may also focus on the suitability of the legal engine that is meant to combine forces in order to bring together capital and labour resources with the aim of maximizing output, minimizing cost, and improving the welfare of all those involved in the production/distribution process. Such legal entity must be based on beliefs as indicated already above in the brief assessment of industrial democracy, ESOPs, and the economy of communion model.

The role of co-operatives in the Maltese Islands following Malta's membership of the European Union may be assessed in relation to the move from 'personal to impersonal exchange' (North, 1999). 'Personal exchange' refers to a world in which people deal with one another in small-scale economic, political and social activity, where everybody knows everyone else, and where it pays to co-operate. In such a world, transaction costs are low; production costs are high because it is an environment of small-scale production that excludes economies of scale. In 'game theory' terminology, human beings co-operate when they play a game over and over again; where there is no end game; when they know the other parties to the exchange and when there are small numbers.

'Impersonal exchange' is based on a global perspective in which a large number of people are involved and transactions may not be repetitive. It is a world where one's dependence rests upon people one does not know, spread over a wide geographical area. In such a context, 'games' are played differently: it pays to defect. Institutions evolve in such an impersonal exchange environment in order to render co-operation worthwhile encouraging players not to cheat, steal or lie.

The co-operative set up may be considered an intervening mechanism that keeps the many producers/consumers together, focused on set objectives, with the specific aim of minimizing defection, cheating and theft. Co-ops have to be seen not only as economic institutions, but also as political institutions. They have to embody a corpus of beliefs on which economic behaviour can be customised to ensure the group's economic survival in a highly uncertain world. Technologies, the degree of competition in the respective markets, government policies, and operational design and thrust: all these change. And so co-ops, as intermediary institutions in the long process involving the passage from 'personal exchange' to 'impersonal exchange', have to adapt in time to be resilient, effective, and, so, survive. But institutions generally change very slowly and they may be overtaken by events!

Besides, real-world co-ops operate in different industrial sectors. And some sectors may rely on institutions more than others. The dependence on institutions, the enforcement of contracts and property rights, is a technical feature of the production process in some industries. Hence, those sectors that are served by 'better' co-ops may gain from productivity and hence have an edge in international trade. Conversely, poorly organised co-ops will result in higher unit cost and a loss of comparative trade advantage. The poor quality of institutions will be reflected in lower productivity in the institutionally sensitive sectors. A competitive trade environment renders bad institutions more costly; a freer trade environment demands more efficient institutions (Levchenko, 2004).

In sum, there are several legal forms of organisation that encompass principles of solidarity, ownership and the sharing of value added. The utility of such organisations changes over time with economic development. Their effectiveness is influenced in part by the policies implemented; these reflect a set of beliefs that animate them. Free trade demands sound institutions; ones that identify clearly a set of objectives and that are organised in a way as to render such objectives attainable. Poor organised units generate high unit costs and a loss of comparative advantage. The survival of these economic structures depends on their successful adaptation of these units over time. To survive, therefore, co-operatives, being legal entities with explicit efficiency and solidarity-related objectives, must prove to be effective instruments that bridge the move from a 'personal exchange system', where it pays to collaborate, to an 'impersonal exchange system' where it pays to defect. The significance of behavioural relationships that embody a culture of efficiency and solidarity is examined below.

2. Economic Efficiency, Welfare Generation and Co-ops

Economic theory defines a 'first-best' position as a situation in which it is not possible to improve someone's welfare without making someone else worse off. This condition is attainable in markets for goods and services that are made up of large numbers of buyers and sellers, who have knowledge of the ongoing business activity and who, individually, cannot influence price. In such a 'perfectly competitive market' individuals respond to the price signals they receive and decide on the quantities they want to purchase, in the case of consumers, and the quantities they want to supply at a profit, in the case of producers.

It is an economic scenario based on choice and competition. Limiting choice and competition, therefore, tends to induce waste of economic resources thereby affecting negatively the process meant to maximise output and, in turn, enhance personal welfare. Hence, when choice and competition are curtailed or even unavailable, for valid reasons, it pays everyone to construct markets for exchange on contractual obligations entered into between producers and consumers through the intermediation of a state regulatory agency. Such obligations aim to ensure value for money for consumers and a fair rate of return for monopolistic producers.

A perfectly competitive market structure tends to exert pressures on producers to operate at levels that yield simultaneously three distinct conditions regarding price and costs. First, producers may aim at maximizing profits. This objective may be summarised by the operational condition where the change in revenue arising from the sale of the last unit produced (Marginal Revenue) will just cover the cost to produce that unit (Marginal Cost). To simplify, it is usually assumed that the computation of costs include all costs incurred in production, that is both costs that are borne by the producer and any other costs that are generated in the process, including an estimate for inconvenience to neighbours through noise and other discomfort!

Secondly, since producers are price takers they equate their marginal cost to the market price. This condition means that consumers are paying a price – hence, exchanging resources equal to the monetary value reflected in the price – that is equal to the value of the inputs applied by the firm in the production of the marginal unit. Such inputs include also an imputed value for a fair return to entrepreneurial activity.

Thirdly, because of competition producers are forced to operate at levels that reflect the least unit cost possible. They have to be efficient to survive. It is this least-cost-per-unit value that is charged to the consumer.

The three conditions described above are operated together. They represent a situation where consumers are charged fair prices and so they are not 'exploited'; firms are producing at the least-cost possible with the given technology at their disposal, thus they are efficient; and producers are maximizing their profits. It is a win-all situtation. These conditions are summarised below.

Marginal Cost = Marginal Revenue (MC = MR) (1)
Marginal Cost = Price (MC = P) (2)
Minimum Average Cost = Price (ACmin = P)(3)

When there is only one producer, or when many producers combine forces to exert pressure on the prices obtained in the market, the above conditions may not hold unless a regulatory agency forces producer behaviour to 'correspond' to any one of the conditions expressed in equations (1) to (3) above. For example, a monopolist that aims to maximize profits (and meet condition (1)) will not meet conditions two and three. Hence the perception that monopolists 'exploit' consumers by charging prices that exceed the marginal costs of production, and that monopolists are inefficient because they do not extend their operations up to the point where unit costs are at a minimum.

The same may be claimed for a number of producers that come together and bear influence on the market. Co-ops and producer organisations may fall under this category; the observations made by Malta's Commission for Fair Trading, quoted above, point at this possibility. Under such conditions, there arise welfare losses and an inefficient use of resources. Diagram 1 illustrates this loss for consumers and for society in general.

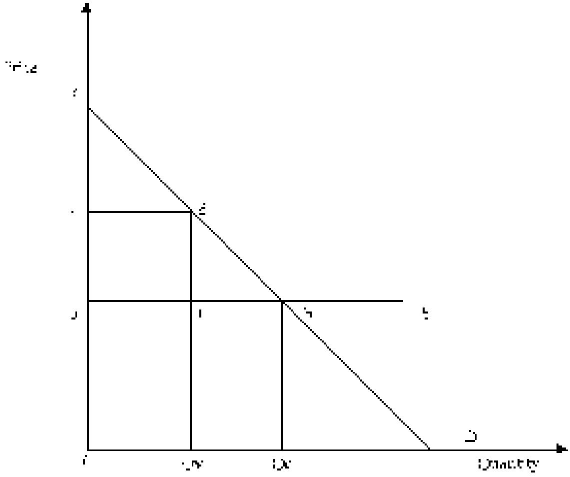

Diagram 1

Under a perfectly competitive market setup, output is Qc at a price of Oa per unit. Total money outlay equals ***Oa.Qc***. But the total worth to consumers exceeds this value by the amount that they consider that units Qc are worth to them; this value is equal to the money they pay to purchase the commodities and the additional worth, measured roughly by triangle ***abc*** that represents the 'hidden surplus'. This 'consumer surplus' approximates a value equal to ***0.5(ac.Qc)***.

The value of sales under the monopoly market conditions equals ***Qm .Oe***, of which ***afde*** represents 'excess' profits or 'monopoly rent', that is profits that arise because a monopolist controls output, thereby keeping price high, in order to maximize profits. The consumer still enjoys a surplus represented by triangle ***edc***, which is much less than the former surplus ***abc*** obtained under the perfect competitive market conditions. Part of the former surplus is transferred to the single producer; this is equal to the area represented by rectangle ***afde***. But a value equal to triangle ***fbd*** is lost because no one appropriates it. This value represents the 'deadweight loss' arising from the switching from a perfectly competitive market structure to a monopolistic set up, from a business environment where those who participate in the exchange are price takers to one where one/some producers can influence price.

But apart from this deadweight loss, there may be other resources that are inefficiently used in order to consolidate the monopolist's position. The monopolist may allocate resources up to the value represented by rectangle ***afde*** in order to preserve the market dominance position. The initiatives undertaken to shield monopoly rent, such as lobbying to support the status quo and contain competition, are referred to as *"directly unproductive profit seeking" (DUP)*. Such lobbying is carried out to influence trade policies by pressuring for tariffs and quotas, or to obtain a bigger share of government spending, or to fall under tax-avoidance categories, thereby escaping from taxation; or, still, to go for government regulation. The resources dedicated by firms in this manner represent a loss to society over time. They are difficult to identify, because they generally end up being disguised under the setting up of long-winded bureaucratic procedures. In the long run it pays no one to support such measures, especially organisations that are inspired by the principle of solidarity.

When for valid reasons there may be situations where one or few producers can meet the demand of consumers, it pays to think of such market situations in terms of a long-term contract between those who provide the service and those who buy it. Owing to uncertainty and other problems, both parties to the contract limit future options in order to achieve optimality over time. Contracts serve to provide procedural mechanisms for adjudicating future contingencies. By increasing the producers' right to serve makes the contract more attractive to producers while simultaneously making the contract less attractive to consumers. The opposite holds if the consumers' interest in the right to be served is accentuated. A regulator can act as a proxy for such agreements. Long-term contracts are difficult to define and enforce because it is costly to delimit, ex ante, their many provisions. A monitoring agency can continually define the relationship between consumers and producers over time in much the same way that courts of law continually interpret rights and obligations of citizens vis-à-vis other citizens and the state.

Such a contractual environment expects an efficient regulator or regulators. These may refer to consumer protection, co-op supervision and business carried out by credit institutions, to name just three. Efficient regulators aim to ensure fair dealings at any one time, and anticipate changes that are on the legislative horizon. The aim is always to ensure a healthy development of a sector or its transformation according to the international business development. A world that is moving towards a 'freer', more competitive, trade environment, is bound to exert pressures that many traders accustomed to operate in sheltered business milieus may find incomprehensible and be lost unless guided properly and in time. A combination of far-sighted leadership at the regulatory agency and at the level of the firm - the co-op at local and regional level in the case under analysis – will go a long way to chart a profitable future not necessarily for all those active at a point in time but for all those who can compete.

Such a position may be addressed through reference to diagram 1. A productive unit accustomed to operate in a sheltered environment will, more or less, act like the monopolist. It aims to maximize profits by keeping firm control on production and lobby for measures that discourages deviants and the formation of competitive alternatives. Over time, its price policies approache Oa in Diagram 1, with output represented by Qm. However, the liberalisation of the market especially following the opening up to regular international trade transactions, will eventually force prices down to their international equivalent, say those represented by Oa. If the structure of production is such that the once-sheltered producer can continue to operate at a profit, notwithstanding the competition, then efficiency will prevail, the consumer gains and a healthy trade environment will develop in the long-term interests of all involved. However, if international trade renders possible prices that are lower than Oa, and producers find it difficult to adapt, then it is a signal that resources have to be transferred elsewhere, where they can generate sustainable, positive and fair rates of return.

Co-ops are meant to be above all competitive, autonomous enterprises. This economic objective is crucial for long-term success and it is therefore lasting. Competitive units can be identified when they are able to produce the goods and services consumers want to buy at the right price at the right time. Competition implies the viable, profitable production and distribution of commodities in an open trade environment. In turn, such a trade environment expects a constant search for an enhancement of productivity. The productivity of human resources determines their wages, while the productivity with which capital or land is employed determines the return it earns for its holders. Trading in a quota/tariff-free zone, like the single market of the European Union, demands specialised skills that enable producers to gain advantage from wider markets, provided they upgrade in time to meet the more-demanding consumers' expectations.

In principle, the co-op model, as such, should not detract from such a search for efficiency, unless its 'solidarity between members' may for a time overtake the 'solidarity with the rest of society' and render the co-op insensitive to the trading demands that lie ahead. But co-ops do not exist in a vacuum; they are part of the modern, mixed market economy and, over time, they cannot expect to be given preferential treatment or be 'positively discriminated' by policy makers. They do need a regulatory environment that recognizes their special form of organisation/ownership, one that does not pit competition rules against co-operative rules. Otherwise, it will be difficult for co-ops or producer organisations to operate at all. Shareholding and 'employee ownership' in its various forms must be given enough space to operate in the interest of economic efficiency. It will be up to time to decide which of these institutional paradigms best suit different markets and different regions.

What co-ops themselves have to constantly monitor is the balance they have to maintain between striving to be efficient and aiming to generate solidarity. The underlying desire of members to support one another and to grow together may be stretched too far to the extent that members' interest will supersede the common good. In this case the co-ops' rationale for being will be challenged and other means of supporting their members may be considered by society at large. This is especially so if economic units benefit from special fiscal incentives, like tax concessions/rights or financial transfers, for registering themselves as co-ops.

Alternatively, the co-ops have to be on guard not to allow their statute and related benefits recognised at law to be abused of by their members. This can happen when members are no longer loyal to the group and participate in market transactions in direct competition with the co-op. Such situations represent ‘free rider’ positions; it is in nobody’s interest, except of those members who behave in this manner, for the co-operative set up to continue functioning. In such circumstances, the co-op will not contribute to the long-term economic efficiency goal of a community. Therefore, the ‘solidarity appeal’ of the organisation has to be constantly under check.

In sum, economic efficiency and fair-trading can be reconciled through choice and competition. Successful enterprises that can meet consumers’ demands at a profit can be established once they compete internationally. If such trade cannot be undertaken, for various reasons, then monopoly production can be seen as a contractual relationship between the producer and potential clients. In such a business environment, government agencies act as regulators; they ensure value for money for consumers and a fair rate of return to producers. Co-operatives are private enterprises; they have to aim for an efficient production just like any other form of organisation. But there has to be a clearly defined legal environment that accounts for their special form of ownership. Otherwise, their search for profitable, efficient production will be impeded by legal constraints that do not meet their special characteristics. However, co-ops have to utilise their collective strengths in order to strive continually for economic efficiency, apart from seeking the interests of their members. Solidarity should enhance such a drive and not act as a drag over time. If this happens the very existence of the co-operative will be put at risk. The role of the solidarity/democratic principle is now examined.

3. Solidarity, Decision-making and economic dynamics

Solidarity is fundamental for the setting up and operation of co-operatives. Solidarity expressed by members of a co-op first and foremost towards one another. And solidarity that extends to members of other co-ops. In a co-op, a member's welfare is considered to be dependent not only on the goods and services he or she produces and/or consumes but also on the welfare of other members. An increase in one member's production or consumption enhances personal welfare. But so does an improvement in a fellow member's production or consumption; it leads to a higher welfare level for all. This may be summarised in the following equation:

$$U_i = f(X_i, Y_i, ; Q_i; X_j, \ldots; Q_j \ldots;) \qquad (4)$$

$$dU_i/dY_i > 0 ; dU_i/dQ_i > 0; dU_i/dX_j > 0; dU_i/dQ_j > 0$$

where:	U	= Welfare
	X, Y	= goods and services consumed
	Q	= output produced
	i, j	= individuals i and j

Indeed, if one were to take a wider view of this inter-personal support, then one can integrate vertically the solidarity process to include both the suppliers of services to an economic unit, and the users of services/goods exchanged by the unit. They fall under 'individual j' in equation (4). This is the approach adopted by the Economy of Communion model described in section 1 above.

Self-interest will be harnessed to the increase of material output of society but the link is reinforced through a co-operative system that guards against abuse and exploitation. The reward to self-interest is made more secure and comprehensive by the operation of secondary co-operatives;

they give the community an institutional claim to moral achievement that may be considered sounder than the self-regulating force of the market system (Hoover, 1992). While there may be no intrinsic reason why a co-operative would behave in a more socially responsible way than a capitalist firm toward, say, the environment, the conditions for prudence and long-term vision are evidently in place.

These views contrast with another vision of self-discipline that is engendered by the market place (O'Keeffe, editor, 2004) Markets are seen providing a larger moral dividend than attempts at altruistic preaching on behalf of moral sentiments. Self-interest, the main motivating factor behind economic decisions, is not the same as the selfishness that is often said to underpin the market economy. People's response to profitable opportunities says nothing about their moral outlook or about their deepest motives. Entrepreneurs are motivated by a whole range of subjective desires; but even when profits are used to achieve purely materialistic pleasure the market activities that generate profits are likely to give rise to some social benefit in the meantime.

Given this uneasy intellectual stand regarding the role that incentives and solidarity may have, in their various formats or degrees in the productive and distributive systems in a community, it is pertinent to raise several issues. Some have already been identified in the preceding section. First, is solidarity conducive to efficient production? Will market pressure, following a country's participation in a single market or in a freer world trade environment, induce a radical reconsideration of the co-op model and push it on lines of the standard hierarchical organisation? Is internal deterioration, such as bureaucratic drag, inevitable? How does the evolution of an extensive welfare support system, backed up by taxpayers' monies, affect the member/co-op (individual-collective) allegiance over time? Can co-ops, which are explicit value-based organisations, maintain their 'solidarity cum integrity' over the years?

Research suggests that firms that base their organisational structure on co-operation do produce positive results; independent of the form 'cooperation' takes. Research also suggests that the transition from a co-operative to a hierarchical firm is a possibility as markets expand and co-ops grow bigger. Besides, co-ops that fail to adapt to changing market conditions will be lethargic in their response to the emerging challenges arising from more competitive environments; their decision-making processes may be too slow to provide quick responses in fast-changing markets. In turn, the educational-social support objectives, that could have triggered the formation of co-ops in the first instance, may be replaced by the extensive intervention of state-funded schemes that prop up households' income and consumption. This means that the social objectives of co-ops will have to be reconsidered as government commitments to society expand and per capita incomes increase. Under these conditions, the aspirations of the individual members with regard to the co-op and society at large are expected to change. Under these conditions, the economic objectives of efficiency and long-term viable production become paramount.

If institutions survive by adapting to change in the environment in which they operate, then co-ops cannot be considered an exception. The ideals on which co-ops are founded, such as economic efficiency and participatory democracy, can be interpreted differently at diverse times and places. Similarly, racial, political and religious neutrality, fairness in surplus distribution, and continuous education of members, the principles on which co-ops are structured, may be subject to interpretations as societies evolve.

Modern societies are changing. Secularisation and consumerism in many countries fuel the careerist aspirations of young people. The advancement of women in the labour force increases competition in the labour market, at a time that the rhythm of life is getting faster and people are more independent-minded. These traits may be considered a threat to social solidarity, a value that lies at the core of the co-operatives' constitution.

Unless co-ops are to become utopist organisations, they have to match solidarity with entrepreneurship, capital formation and a speedy response to trade cycles and the opening up of markets. At the same time, they have to consider carefully emerging differences in the interests of members/workers and managers. Successful co-ops, like Mondragon, have been searching for viable answers to such queries. They approached them directly. Failure to do so will lead to an anachronistic institution that will find it difficult to match the advancements made by other forms of industrial organisation. Co-ops have to be guided by the market structure in which they operate. These structures are conditioned by two factors: the product/service being exchanged and the number of producers that compete to meet the forthcoming demand. There cannot be one answer that fits all questions, as the situations illustrated in diagram 1 above indicate.

Similarly, the way co-ops treat their members in decision-making may have to be addressed. Co-ops pride on the fact that all members are considered equal irrespective of turnover or 'size'. Every member has one vote. This is in strong contrast with the voting rights in a capitalist firm. Voting rights, and therefore weight in electing members that spell economic strategy and oversee its implementation, reflect personal commitment in the provisioning of capital in a joint-stock company. But a similar system with differentiated voting rights, proportional with every member's turnover but possibly capped, can be implemented for co-ops as well. Such decision making/ voting systems are already operated by Dutch agricultural co-operatives, for example (van Diepenbeek, 2000). This voting approach is consonant with business principles and with the liabilities and risks that are proportional to every member's turnover. Such an approach could support co-ops' development, because it places decision weights in relation to the risk undertaken. If such voting rights are capped, then a degree of solidarity will be maintained while individual commitment to an economic activity will be recognised at the same time.

In sum, since objectives and the means to attain them may change over time, institutions – that is, forms of organisation – have to adapt with them. Co-ops have to undergo a continual assessment to evaluate the economic and social targets that they are meant to achieve in the context of changing members' wealth, cultural achievements and related tastes and aspirations. Because of this evolution, methods of internal co-op matters, including voting rights systems, may have to be adapted to enable the co-ops to be both profitable institutions – a long lasting objective – and supportive of members' needs and, also, the needs/aspirations of those with whom co-ops carry out trade. Response to changing world trade scenarios means the creation of adequate capital base, fast response to business decisions, and flexible operating procedures. It is in this context that the meaning of the social objective of 'solidarity' has to be expressed and transformed into everyday reality.

4. Insight for Maltese Co-ops in the European Union

The discussion so far established a series of considerations that may be followed in assessing the desirability of forming effective organisations based on the co-operative model. Firstly, institutions play an important role in a community's social and economic development. They facilitate trade through the enforcement of laws, the upholding of property rights, the rewards accruing to those who undertake initiatives, and, depending on ethical beliefs, the expression of various degrees of solidarity in the supply or purchase of goods and services.

Secondly, in a bounded trade environment, where 'personal exchange' takes place, there are rewards in collaboration. In a world of 'impersonal exchange', based on a global perspective, it pays to defect. In such an environment, institutions evolve to render co-operation worthwhile encouraging people not to cheat, steal or lie.

Thirdly, different industrial sectors rely on institutions more than others. Institution-dependency is a technical feature of the production process in some industries. Sectors that are served by better institutions (co-ops, in this case) may gain from productivity and hence gains an edge in international trade. Conversely, poorly organised co-ops will result in high unit costs and loss of comparative advantage.

Fourthly, in a market of price takers (perfectly competitive trade set up) output and prices tend to be efficient and fair. In markets where traders control price or output, there is a tendency for output and prices to be sub-optimal. However, such second-best positions may be unavoidable, at times. In this case, contractual relationships, interpreted over time through an impartial and efficient regulator, can take account of the interest of both producers (ensuring a fair rate of return for risk and capital committed) and consumers (ensuring value for money).

Fifthly, beneficiaries of monopoly rent can be tempted to use these windfalls to sustain their hold on the market. They use such resources to lobby for the extension of their long-term interests. These include favourable tax-avoidance rules, pressure for trade protection and other forms of regulation. Such activity is considered unproductive and not in the long-term interests of a community. It forestalls economic growth. Co-ops are meant to be competitive, autonomous enterprises. But they may not be so, for various historical reasons. They might have relied for too long under a government's tutelage. Such a set up will not be conducive to a healthy institution that can withstand the forces of competitive trade, as argued in consideration number two above.

Sixthly, both the market and the 'solidarity criterion' may be conducive to tempering greed and to derive long-term prudence in business transactions. If co-ops are not to be turned into utopist organisations, they have to match solidarity with entrepreneurship, capital formation and a speedy response to business cycles in a free trade environment. Strong management, timely decision-making, commitment to capital injections and loyalty in transactions can demand a system of differentiated voting rights. This goes against the traditional co-op set up of 'one man one vote'. Capping such voting eligibility can combine efficiency/loyalty considerations and solidarity underpinnings.

These six general observations may be applied to the present situation of Maltese co-ops, in particular to the agricultural units. In turn, they can be considered in the context of an evolving European Union–Rest of the World trade negotiations at the World Trade Organisation. Malta is bound by such arrangements and by EU-Mediterranean countries' bilateral settlements.

In a small community, 'personal exchange' behaviour is expected to dominate trade transactions. Yet co-ops in Malta seem animated by a spirit that encourages defection, the hallmark of 'impersonal exchange'. There have been too many internal misunderstandings, where members compete with their co-op, carry out trade outside the co-op set up and resort to the organisation to benefit from guaranteed prices that the co-op establishes for its members.

This 'unco-operative behaviour' calls for an explanation. One possible reason for this apparent lack of the 'spirit of belonging' may have arisen from the way in which the co-ops, especially those considered most successful, have evolved over the past few decades. Several local co-ops operate through a top-down structure rather than through a base-top direction. They rely on government support, with public officials having a determining role in the running of the affairs of the co-op movement, in particular the Co-operatives Board and the Central Fund. A top-down approach will find it hard to instill solidarity, an attitude that is basically personal. Such a pseudo-bureaucratic organisational set up could have led to indifference mood that has been observed among members.

In turn, such an attitude gave rise to the search for alliances, characteristic of the political market, rather than to the search for economic efficiency that is the hallmark of commodity markets. So, splinter groups in the co-op movement would not seek common ground on which differences might be resolved. Instead, they vie for official recognition to consolidate their position. Public sector support could mean cash injections, tax concessions, and possibly human resources. Though effective in the short run, such an approach may not instigate a process of continuous search for new markets and for innovative ways of carrying out existing operations.

The switch from such an organic milieu to one based on the least-cost principle would be difficult to implement, especially at a time when there exists already a plan during which long-awaited structural reforms have to be undertaken. Furthermore, an ageing membership does not help in the circumstances! But the present conditions that see the commitment of the Maltese government circumscribed by rules on competition in the Single Market and fiscal consolidation among member states in the European Union could prove to be the long-sought catalyst in the co-op movement. For the first time in many years, members have to come together of their own initiative to chart their future, because they feel the need to collaborate.

Such action stands in contrast to the approach whereby participants were called to come together following some form of government intervention. Whatever structure is set up will represent a base-top relationship with the base identifying the industrial format it seeks to operate and the managerial structure it deems profitable to implement. If the co-op (efficiency with solidarity) model is adopted, it will be an own decision, chosen freely on the assumption that it is the best 'alliance' on which to base a stable efficient production set up that can compete successfully in a wider trade environment. Co-operation will have to assume a new meaning in the local context. It cannot stand for collusion among interested parties to keep other players out of a market. It would mean bringing in as many players possible, strengthening the capital and skill base, and hiring the leadership resources that can induce the best elements in the group. This is important especially in the context of co-operation across Member States.

The European Union has around 300,000 co-operatives, employing 2.3million and providing services to 83.5million members. Cross-border cooperation between co-operatives has been hampered within the European Union by legal and administrative difficulties. Council Regulation of the 22nd July 2003 (Official Journal of 18th August 2003 – L207) provides co-operatives with the legal instruments to facilitate cross-border and trans-national activities. The Statute provides also an ideal legal instrument for companies of all types wishing to group together for their common benefit, such as to access markets, achieve economies of scale or undertake research or development activities. The Statute enables five or more European citizens (physical persons) from more than one Member State to create a European Co-operative Society.

Such a scenario represents a radical break with the sheltered mentality that prevailed for many years in many production units in the Maltese Islands, co-operatives included. It represents a break-through in a drive at excellence that, at the same time, attests to the need to instill collaboration even across Member States to achieve this objective. But such a vision expects a lucid understanding of the forms of organisation involved. And the co-operative model cannot continue to be regarded an 'afterthought' if it is to become a positive pro-active medium for economic growth and social harmonisation. The implications at law and in every day realities have to be understood and accepted by all participants.

The co-operative model of organisation cannot be applied 'in extremis' to reach an objective. The Maltese government is recommending the formation of housing co-operatives as a measure "assisting vulnerable groups in attaining suitable housing"(Management Efficiency Unit, National Reform Programme, 2005:54 – 19.3.5). Government is also proposing to "provide incentives to co-operatives to get teams of people forming such organisations" in an attempt to develop new sources of jobs in services. Indeed, this measure falls under a heading 'incentives to *employers'* (italics added) to 'promote the creation of full-time jobs' (Management Efficiency Unit, National Reform Programme, 2005:54 – 19.3.6). Co-operatives apparently are seen a 'deus ex machina' solving all economic and social issues at hand!

It takes much more to set up an effective co-operative. This is especially so when those who are proposing such measures intend to coordinate joint-stock companies and co-operatives. In the same document on National Programme Reform, government aims to encourage start-up business within schools. "The current scheme of school co-operatives (SCOOPS), which is open to students in secondary education and the Young Enterprise scheme, provided in the post-secondary period, will be reviewed with a view to identify potential improvements in both schemes and more coordination between the two schemes" (Management Efficiency Unit, National Reform Programme, 2005:42 –M15.15). Joint stock units and co-operatives take their cue from a different philosophy of organisation. Therefore they are to be seen as 'competing' models of organisation involved in the generation of economic output.

It will be interesting to discover the ways in which two distinct models of organisation can be 'coordinated'. This is especially so when co-operatives are being recommended at junior secondary school, and joint-stock companies promoted at pre-university institutions. It seems logical to assume that young men and women will be more enticed with what they are taught later on in life than what they learn when young. Of course, it is not the units as such that are 'right or wrong'. It is the absence of a clear decision of what policy makers want to achieve, to boost co-ops or to support the joint-stock model, which stands out. This approach could well be the outcome of the historical perception by public sector officials of co-operatives.

Surely, policy makers have to appreciate the distinct characteristics of these forms of organisation. Otherwise Malta will continue to have co-ops that are structured on the Co-operatives Act but no real co-operatives, ones that inspire themselves from the solidarity criterion and apply bonding in order to be efficient. In this case, the institutions would represent a mirage, with no substance. There will be no effective institution to focus members' energy to achieve a common aim.

5. Summary

Co-operatives are organisations that are inspired by basic beliefs in solidarity and economic efficiency through which they aim to improve the welfare of their members. They belong to a group of organisations that aim to promote economic growth and fairness in the distribution of generated value added. Like other institutions co-operatives have to prove themselves to be useful media to reach the proclaimed objectives and, in doing so, enhance other people's welfare.

Similar economic and equity objectives may be attained through other forms of organisation operating through market systems and government programmes that redistribute income. Therefore the co-operative paradigm has to compete with these other forms of industrial structures in order to be identified by potential members as effective instruments in a globalised trade environment. Such a scenario demands a persistent drive towards the least-cost mode of production and providing value for money for consumers. Solidarity among members is meant, in part, to induce such an organisational framework.

Maltese co-operatives gained access to government support in cash and kind. But they seem to have missed, over time, the allegiance of their members. This result raises the query of the choice of the co-operative model as a medium of change, competitive performance, and individual support in Malta and Gozo. It seems that this model has been misrepresented in the past and a close consideration of its fundamental undertones is a necessary condition for its survival. Such reconsiderations could be extended to the possibility of applying differentiated voting rights, perhaps capped. This approach differs from the 'every member one vote' exercised under Maltese law.

Once recognition of the basic principles on which this model stand occurs, then one can proceed to assess the usefulness of cross-border co-operatives or company co-operation with participants from various Member States in the European Union. Such a cross-national model demands a culture change in Maltese operators, particularly in agriculture, who have to date sought protection, via the co-ops, from domestic and international trade competition. In future, the co-op has to become an instrument that enables fair competition for both producers and/or consumers. This can be achieved if life and vision of co-operatives arise from 'below', from a feeling among its potential members that they can support one another, think collectively, and act accordingly in order to compete in free markets. Short of this multiple vision, a unit claiming to be a co-operative will be assuming the legal structure of a co-op but will fail to live up to the co-operative spirit.

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PART TWO

INTERNATIONAL EXPERIENCE, THE MALTESE SET UP AND PRODUCER ORGANISATIONS

JOHN ROUSE and JANOS JUHASZ

FAO EXPERIENCE IN AGRICULTURAL CO-OPERATIVE DEVELOPMENT ASSISTANCE

1. Introduction.

Reducing rural poverty, promoting sustainable rural development requires social capital, especially the existence of viable group-based enterprises, such as co-operatives, that help small producers reduce their transaction costs in accessing services and markets to improve their incomes. The same organisations also play an important role in developing rural communities and in introducing more democratic forms of decision-making and self-governance, issues that are becoming increasingly important in modern development.

Since the beginning of human history, small producers have organised themselves co-operatively in various ways to reduce their transactions costs in pursuing common economic goals. Although these forms of cooperation, which range from small informal self-help groups to larger formal ones organizations like producer associations or co-operatives, share many similar features, they also show substantial differences from one region to another depending on each country's different history, traditions and problems. That being the case, the definition of what constitutes a "producer group, "union," "association" or "co-operative" may differ significantly from place-to-place. For example:

- In *North America and Europe* agricultural co-operatives and producer groups were largely private and voluntary collective self-help initiatives of small producers. Government role was minimal. Due to the decentralized development of the North American frontier in the post-colonial period where each state set up its own laws governing such organisations, development of these groups has been significantly varied and innovative.
- In *Latin America* traditional indigenous communal and labor exchange groups, church and trade union-promoted groups including credit unions, transport co-operatives, production and consumer co-operatives came into being. Most of these were private initiatives but some agrarian reform-linked agricultural co-operatives were also established. Nevertheless, the majority of the latter ones also remained fairly autonomous organisations.
- In *post-colonial Africa and Asian countries* agricultural co-operatives, especially those grouping small producers in high value export crop sectors (coffee, tea and cocoa) were largely government-controlled producer groups formed to organize small-holder production and facilitate marketing through government controlled Marketing Boards. In most cases member participation was not voluntary but mandatory and the multi-tiered structures (primary society, district co-operative union and national federation) were used as instruments of government policy for rural surplus extraction and political control.
- In *Central and Eastern European (CEE) countries*, most

> producer group enterprises were also private initiatives in the pre-communist era but once under communist control, these structures were "captured" by the state and quasi-nationalised. In agriculture, instead of service co-operatives, large-scale, parastatal co-operative farms were established. With the only exception of Poland, these became the dominant form of agricultural production organisations in all CEE countries.

Two types of rural producer organisations that have been largely successful in safeguarding their autonomy and independence regardless of the region in which they are located have been the *caisse populaires, and co-operative savings and credit societies*, or *credit unions as they are sometimes called*. In addition to North America and Europe, these organisations are also widespread throughout Latin America, Africa and Asia.[1] Because of their heavy emphasis on mobilizing member savings as the primary source of funds to finance growth, instead of reliance on outsiders, credit unions have managed to maintain their economic independence and operational autonomy from government.

2. Brief history of FAO activities in support of agricultural co-operative development

Ever since its founding in 1945, one of FAO's responsibilities has been the strengthening of all forms of collective economic action of agricultural small producers through the delivery of normative and policy advice to governments and other development agencies. Yet, it is important to note that its approach to promoting group-based enterprises has undergone a number of changes since that time in response to altering circumstances. A review of FAO documents from 1945-1975 shows that its approach to rural producer organisation development has evolved from a top-down methodology of organisation development in the early years to a more participatory, bottom-up one, especially after the World Conference on Agrarian Reform and Rural Development (WCARRD) held in 1974.

i. Post- colonial period (1945-1974)

In its first years of operation, FAO was to a large extent staffed by technical personnel drawn from the former British, Belgian, Dutch and French colonial services. This was not surprising in view of the fact that most of these former colonial government bureaucrats and technicians had spent decades working in developing countries and possessed in-depth knowledge of the local cultures and potential for institutional change. On the negative side, many of them brought with them paternalistic, top-down perspectives towards co-operative development that were quite different from the farmer-led, participatory perspectives of co-operative and producer organisation leaders and promoters in developed countries.[2] Nevertheless, the "top-down, post-colonial perspective" held sway through the early 1960s and had a great impact on the FAO approach to co-operative development assistance

Cold War politics and the US-funded Alliance for Progress development assistance programme during the 1960s and early 70s also had a major impact on FAO's approach to producer group-enterprise development. US policymakers regarded that the inequities existing in rural areas in many developing countries, especially in the Latin American region, were a major source of popular discontent and posed a threat of communist takeover. To counter this menace, the main focus of Alliance for Progress aid focused on promoting the growth of more democratic and participatory rural institutions in the Third World. This led to a major increase in donor funding of rural institution-building initiatives in developing countries, much of which was channeled through UN specialized agencies like FAO.

ii. The UNRISD Study and the AMSAC approach (1975-1988).

But by the early 1970s, criticism of UN agency mishandling of some of this foreign assistance had begun to mount. In 1975, the United Nations Research Institute for Social Development (UNRISD) published a comprehensive study entitled *"Rural co-operatives as agents of change: a research report and a debate"*.[3] This study had a major impact on FAO's perception on development assistance and caused a lot of rethinking within FAO on the best way to promote sustainable rural development using group approaches. It provided compelling empirical evidence that the traditional approach to co-operative development in LDCs – with some exceptions – had largely benefited rural elites and governments, and not the poor.

Two other massive studies of rural organisations by Gow et al (1979) and Esman and Uphoff (1984) during the same period confirmed many of the UNRISD findings.[4]

FAO quickly responded to the UNRISD criticism with a three-pronged approach: (1) through the launching in 1974 of the Rural Organizations Action Programme (ROAP), a research programme that aimed the main objective of which was to identify more efficient *group-based* methods to reach the rural poor and ensure their more active participation in the process of rural development; (2) through the inauguration of the Small Farmers Development Programme (SFDP), a pilot programme that pioneered the introduction of a new small informal group approach to producer organisation development in a number of Asian countries; and (3) through the establishment in 1978 of a new approach to agricultural co-operative development, called the Appropriate Management System for Agricultural Co-operatives (AMSAC) Programme which attempted to transform traditional agricultural co-operatives into more competitive business enterprises benefiting small producers. While the AMSAC emphasis on the business rather than the social dimension of rural producer organisation development was much needed, the approach remained government-led and continued to rely heavily on government-dominated national co-operative apex organisations for its implementation. Even though FAO poured a lot of energy into developing the AMSAC programme, donors saw very little that was new in the approach, therefore no projects emerged and by 1985, the programme was already dying.

iii. Decline in overseas development assistance (ODA) for agricultural co-operative development and the globalisation of trade (1988-present)

The fall of the Berlin Wall in November 1989 marked the end of the Cold War but also signaled an increased emphasis on donor-driven structural adjustment and privatisation programmes in LDCs and a gradual shift in the volume of ODA away from Africa, Asia and Latin America and towards Eastern Europe

Nevertheless, support for other more participatory, "non-co-operative" approaches to rural development in LDCs remained strong and became the main topic of discussion at the meeting of the FAO Committee on Agriculture (COAG) in the spring of 1989, which eventually resulted in the approval by the FAO Conference in November 1991 of the FAO Plan of Action on People's

Participation in Rural Development (PPP). Ironically, in spite of the excitement about PPP and Rural People's Organisations, extra-budgetary funding from other donors FAO co-operative development dropped from about US$17 trillion to US$10 trillion from 1988-1994 in constant US dollars.[5] Most donor agencies were also faced with budgetary problems and changing priorities of their own which led to a further decline in aid to the agricultural sector and to agricultural co-operatives which has continued up to this present day

In addition to the decline in support for co-operatives, other trends such as the globalisation of trade and the privatisation of state agencies and small producer support services, such as agricultural extension, are creating a new and much more competitive environment for agricultural co-operatives and their members:

- Globalisation of trade and deregulation of domestic markets. Countries are removing barriers, promoting freer trade domestically and internationally. As a consequence, consumers are increasingly able to obtain cheaper goods and services from alternative and more efficient providers. Under these conditions, it is more and more difficult to reserve special privileges or offer special price benefits to co-operatives.
- Privatisation of state agencies and businesses. The new owners of privatised state agencies such as marketing boards and banks are interested in dealing with co-operatives as business enterprises. The co-operatives' roles as government-led sources of supply of agricultural commodities or vehicles of social change are not their concern. To work with these boards and agencies, co-operatives need to be efficient and well-run competitors in the open market.

As a consequence, traditional state-led and state-financed agricultural co-operatives in most developing countries and transitional economies are now going through a painful privatisation process as co-operative markets are liberalized, as development assistance to co-operative development declines, and as governments find themselves less able and willing to play a lead role in supporting and financing these structures. To survive in these more competitive markets, agricultural co-operatives will have to become more competitive and managed as member-led businesses rather than as government led social or political programmes.

3. FAO Experiences and Lessons Learned

i. Agricultural co-operative training programme on participatory institution building, self-reliance and business management (1995-2004)

As mentioned above, if agricultural co-operatives are to survive in liberalised markets and with decreasing subsidies from the state they will have to operate as competitive businesses. Since some of the main weaknesses of primary co-operative societies in developing and transitional countries continue to be a lack of participatory institution building, lack of "self-reliance consciousness" and weak business management, FAO recognized that a new approach to co-operative management training would be required. There was a need for a shift in training focus to participatory learning, self-reliant institution building and business management capacity building. To that end, a more appropriate comprehensive agricultural co-operative training programme, including a set of user-friendly training materials and methods were developed in the form of a replaceable-module *training- of-trainers manual.*[7]

By encouraging greater membership participation in the training process, this innovative manual aims at improving management and familiarizing political and administrative decision-makers with new co-operative development approaches. The training manual is composed of *eight modules*, as follows:

- *Understanding Co-operatives,*
- *Participation & Learning,*
- *Communication,*
- *Organizational Development,*
- *Co-operative Management,*
- *Tools for Planning and Organizing Co-operative Activities,*
- *Participatory Appraisal, Monitoring and Evaluation.*
- *Accounting*

Throughout these modules, the manual deals with ways in which trainers and promoters of co-operatives can support co-operative members and management in the development of their co-operative organisations. Its *objectives* are:

- to broaden the trainers' view of their role, and ways in which they can react to circumstances, and to increase their confidence in their own capabilities. In short, to increase their competence;
- to help the trainer become an effective facilitator and moderator. That is to say, someone who can offer new methods for dealing with problems and tasks, assist in solving conflicts, draw attention to alternatives and assist in the more effective operation of the co-operative;
- to equip the trainer with tools to act as a resource person, providing information to the co-operative organisation, its members, leaders and managers;

- to familiarise the trainer with participatory techniques which involve all parties concerned with the future of co-operative organisations; and
- to support the trainer in the various tasks of raising awareness among co-operative promoters, members, decision-makers, leaders and managers of their problems/constraints as well as in their potentials/capabilities, without taking the initiative away from them.

The manual guides trainers through the process of training by providing a standard structure in each module, including the following units: Objectives of the unit, Key learning points, Teaching strategy, and Reference information. A range of examples and exercises are also given.

There have been two major ways of implementing the FAO agricultural co-operative training of trainers programme and disseminating the Manual: (1) within the framework of the so-called FAO normative programme through training workshops and seminars; and (2) through technical assistance projects requested by individual member countries. In both cases, the impact measured by attitudinal changes and improved technical skills of primary participants has been satisfactory. However, there have been problems with follow-up mainly due to lack of political will and appropriate institutional structure. Nevertheless, the "project method" has resulted in more "tangible" and sustainable outcomes.

ii. Agricultural co-operative restructuring in CEE countries

Transformation of large-scale "socialist" co-operative farms into genuine agricultural service co-operatives has very seldom been successful in CEE countries. "Surviving" large-scale farms most often have been transformed into various types of joint stock companies (Shareholder or limited liability companies.). Some of them, however, have maintained the co-operative form of enterprise and continue to operate as a single production unit. New group-based enterprises, both informal and formal (mainly called associations, producer groups, etc. but very rarely co-operatives), have been established by small farmers that started private farming after the change of the political paradigm. Most of them are now managing relatively small plots of less than 5 hectares.

FAO technical assistance efforts have focused, and should do so also in the future, on this latter group in the sub-region. The main problems of producer group-enterprise development are well summarized in a recent FAO publication: "Proceedings of a FAO workshop held in Prague, Czech Republic in 2001[7] brought together farmers and representatives of farmers organizations and association leaders, government representatives responsible for co-operative and agricultural support services, research, extension and development institutions, from nine CEE countries, Bulgaria, Croatia, Czech Republic, Hungary, Latvia, Poland, Romania, Slovakia, Slovenia. The workshop identified seven key issues influencing the slow development of effective farmer group development across the region, specifically:

1. Inadequate group management, leadership skills and education
2. A general unwillingness by farmers to collaborate and unclear benefits derived from co-operation
3. Insufficient start-up capital
4. A lack of innovation, value added activity and entrepreneurial spirit
5. Generally small farm sizes, and sometimes unclear

land ownership
6. Unclear co-operative legislation and inappropriate taxation policies, and
7. Ineffective marketing and market access"

A special problem of producer group-enterprises, in particular agricultural co-operatives is the negative image that co-operatives have in Central and Eastern Europe due to excessive government intervention and control of these organisation's affairs. Nevertheless, dispelling the negative image will not be easy. One way to improve the public image of co-operatives is to identify "successful" agricultural co-operatives and other producer group-enterprises. In other words, development assistance efforts should not rigidly focus just on co-operatives. There are other self-help organisational options: small producer and marketing groups, contract farming groups, producer unions and associations, investor owned firms, etc. There is a need to adopt a more flexible approach to producer group-enterprise development which would entail developing normative materials and technical service expertise that address group business problems within a variety of co-operative-like producer enterprises.

In this respect, it is crucial that producer group-based enterprises be commercial-focused and have well defined business objectives. Development assistance should make it clear that producer group-based enterprises (including genuine co-operatives!) are *independent* and *voluntary small farmer-run business organisations* which are indispensable for marketing value-added produce by small farmers. Within this, particular attention should be paid to: (1) participatory training and institution building; (2) financial self-reliance (including capital formation) of producer group-based enterprises; and (3) improved management skills and management information systems, with special emphasis on the use of up-to-date information and communication technologies (ICT).

iii. Co-operative capital formation

In response to the decline in government subsidies and loans and other external credits, agricultural co-operatives have begin to see the importance of mobilizing member funds to finance business growth. However, as a number of FAO studies during the mid-1990s pointed out, the mechanisms and incentives to attract member capital were ineffective and reform was needed. This finding led FAO to focus more attention on the problem of co-operative capital formation and to make it another problem focus area for the Organisation's normative work in the field producer group-enterprise development assistance. The member capital issue was also important from two other perspectives. It was well-documented that: a) reduced financial dependence of the co-operative on government and other external sources of debt capital actually led to improvements in co-operative financial self-reliance and in the ability of the co-operative business to act autonomously in the market; and that b) increased member equity stake in the co-operative also tended to strengthen member participation in decision making and reinforce management-to-member- accountability.

Inadequate member capital is a key constraint to successful agricultural co-operative development in many LDCs. A great number of the agricultural co-operatives in Africa and Asia are faced with working and investment capital shortages as donor money and government support disappears.

FAO research on co-operative capital formation began in 1994 in India, Kenya and Guatemala.[8] It was carried out during the 1994-1997 period and led to the publication of the first of two manuals on agricultural co-operative capital formation in 1997. (A revised, more complete manual was published in 2004.) The main findings of the research were as follows:

- Excessive reliance on external versus internal member capital to finance co-operative business growth leads to financial dependence on government and outside donors which limits co-operative business autonomy and makes the co-operative vulnerable to political co-optation and inefficiency.
- Increased member equity participation in financing the co-operative increases top-to-bottom accountability of management.
- Rigid interpretation of the one member-one vote and limited return on capital principles of co-operatives often discourage members' investment in their co-operative.
- Co-operative members should be treated not only as users of co-operative services but also as investors in the co-operative business. Nevertheless, these dual roles of the member are sometimes in conflict and thus require innovative solutions. Numerous case studies clearly pointed out that successful agricultural co-operatives in developed countries and most *caisse populaires* and credit unions in developing and transitional regions treat co-operative members as both users and investors and provide them with incentives to help finance their co-operative's business growthIn contrast, most agricultural co-operatives in in LDCs are still burdened by legislation and practices that simply do just the opposite.[9]
- The studies also revealed that there are three main difficulties in promoting co-operative capital formation:

the horizon problem, the internal free rider problem and the portfolio problem.

The Horizon problem: Since returns on member capital are "limited" (dividends on member shares are low or non-existent), because it does not appreciate in value (member shares are not openly marketed), and since member shares are difficult to redeem or convert back to cash when a member dies or decides to leave the co-operative, there is a built-in bias towards the *member-user* as opposed to the *member-investor*. Consequently, members often prefer to receive the maximum current cash return possible on goods sold or purchased through the co-operative rather than leaving that amount in the co-operative to obtain a *potentially higher future return.*

The Free Rider problem: This problem is manifested in two ways: a) when a member joins a co-operative and benefits from the services of the co-operative but does not contribute his/her fair share in the development of the co-operative; and b) in a mature co-operative, when new members join and pay the same required membership fee and minimum share capital contribution that older members paid but enjoying the enhanced services of a co-operative that was essentially built and capitalized by its older members. Under such a situation, it is understandable why older members would be less than enthusiastic on allowing new members to join and on investing more of their own scarce capital to the benefit of new and "free riding" members.

The Portfolio problem: Since each member has multiple saving and investment needs, which normally include savings and investments both inside *and outside* the co-operative, he/she will be continually comparing the rate-of-return on each of those investments. If the co-operative wants to raise more member investment in the co-operative business to finance its growth, then it must offer a comparatively attractive rate-of-return to the member investor, otherwise it will not succeed. An adequate return can be in the form of better prices received for crops marketed through the co-operative, a better dividend return on purchased member shares, upward revaluation of member shares to better reflect the true net worth of the co-operative, easier "redeemability" of shares, etc.

Improved member capitalisation mechanisms must provide appropriate member investor incentives that address the above three problems. Regrettably, this is seldom the case in many developing countries. Changes in existing co-operative laws and a more flexible and pragmatic interpretation of existing co-operative principles will be required. Fortunately, there are a lot of models to choose from. Indeed, recent FAO studies of this problem indicate that there is much more diversity in the way that co-operatives mobilize member capital than previously thought.[10]

To sum up, co-operative capital comes from three main sources: members, retained co-operative business earnings and outsiders. Finding the right balance between member, institutional and external capital is the main challenge since each source of capital brings with it certain advantages and disadvantages. The higher the proportion of *member share capital*, the higher the member equity stake in the co-operative's business. This helps build member commitment and solidarity and tends to make co-operative managers more accountable to members. The main disadvantage with it is that member share capital in many LDCs earns a very low rate of return, it is normally not marketable and redeemable only at par value. In short, it is not very attractive to members as an investment. Therefore the main problem with many agricultural co-operatives in LDCs is their relatively low level of member capital and comparatively high levels of institutional and external capital.

Institutional capital comes from the retained earning of the co-operative. It's the cheapest form of capital and is an important variable in determining a co-operative's creditworthiness. Having too much institutional capital can cause problems. Since institutional capital is owned collectively by all members and not individually and the co-operative's management is its custodian, it does not generate much downward accountability to members. Furthermore too much institutional capital may actually attract takeovers by other co-operatives or private sector firms.

Finally, *external capital* may be easy to obtain through government or commercial bank loans but it usually ends up creating dependencies on the outside providers that limit the co-operative's autonomy, makes it less responsive to member service demands and results in a loss of member control. To help resolve the above-mentioned capitalization problems, co-operative technical assistance projects at the primary society level should always have a financial self-sufficiency-planning component.

iv. Computerisation of agricultural co-operatives

FAO began working in this technical area in 1999 in Kenya. The initial aim of this initiative was to assess experience in Kenya in computerizing rural co-operatives. One of the research findings from earlier FAO studies on co-operatives capital formation in Kenya was that the low level of computerization in the agricultural co-operatives studied represented a major constraint to improving co-operative competitiveness in privatised markets and introducing more effective methods of member capitalisation. This led FAO to open up a broader area of focus on computerisation of agricultural co-operatives.

In 2002, the Government of Kenya requested FAO Technical Cooperation Programme (TCP) project assistance in developing a prototype computerized information management system for agricultural co-operatives which is now being implemented. In the same year, FAO commissioned three regional issue papers to review agricultural co-operative computerization experiences in the Africa, Latin America and Asia regions. This was followed by an international workshop on the topic at FAO Headquarters in Rome in 2003 which finally led to the publication of FAO's first manual in early 2005.[11] Currently, a joint FAO - Government of Finland project is being launched aiming at expanding this computerization initiative in the Africa and Asia regions.

So far, some of the main research findings on the computerization of agricultural co-operatives in developing countries include the following:

- Agricultural co-operatives are the least computerized of all co-operatives. The problem is particularly serious in Africa.
- While many agricultural co-operatives may not be able to immediately benefit from the advantages of computerization due to their lack of access to reliable electricity and telephone connections, many others can significantly improve their operational efficiency and business competitiveness by doing so.
- Computerisation can bring many benefits, but there are also risks involved. Improved management of business information, more frequent and accurate member reporting, lower running costs, increased profitability, introduction of new computerized

capitalisation schemes, improved access to national and global market information and e-commerce, computer as Internet information portal to rural people are obvious benefits. However, mistakes can be costly, hence computerisation requires careful planning. Up until recently there were no manuals or guidelines specifically tailored to the needs of agricultural co-operatives interested in computerisation.

- Recent changes in market conditions have led to increased interest in agricultural co-operative computerisation. Increased liberalisation and globalisation of markets, the rapid expansion of ICT in developing countries, the success of the FAO MicroBanker software programme for rural banks and credit unions has also led to an increased interest on the part of agricultural co-operatives in computerisation.
- The publication and dissemination of the new FAO guidelines "Computerizing agricultural co-operatives" is expected to generate further demand for FAO technical advisory services in this field. Furthermore, the implementation of the Kenya TCP and the new FAO-Finland Trust Fund project on computerisation of agricultural co-operatives in East Africa are both expected to provide unique field–based learning opportunities for FAO staff to strengthen their technical skills and field experience and make FAO a center of excellence in this area.

v. A new challenge: Contract farming and agricultural co-operatives

Contract farming is a growing phenomenon in many LDCs. This is especially true in the production of high-value agricultural products for export to developed countries as large agribusiness retail firms move backwards down the supply chain to capture added value by securing more dependable sources of supply through such contractual arrangements.

More progressive and educated co-operative members often find the initial contract arrangements offered by such firms, which may include access to credit, certified seed and other inputs, limited technical assistance and higher prices, as economically attractive and begin to deal with these firms directly as individuals, outside the co-operative. Such contracts tend to divert member production, revenue and capital for investment away from the co-operative and towards the "contractor" buyers. In some countries like Zambia, Uganda and Kenya this has resulted in declining co-operative memberships and closedown of co-operatives. Yet recent studies show that such contract agreements could be much more attractive to individual members if they were effectively organized *through* the co-operative.

At this stage, it is still unclear whether contract farming constitutes a real threat to agricultural co-operative survival or whether it can co-exist with co-operative forms of self-help. While members should be free to break rank and do business directly, they should also carefully examine the pros and cons of group contracting arrangements operating within their existing co-operative or outside of it. This is an area that will require further applied research which FAO might be involved in using some of its ongoing projects as research platform.

4. Conclusion

This brief review of FAO experience in agricultural co-operative developmenthas shown that after more than a decade of neglect, there is a growing member country and donor interest in the development of rural co-operatives and rural producer organisations. Donors are beginning to recognize that *sustainable* and autonomous rural people's organisations and co-operative businesses serving small producers play an important role in local economic development and are a key form of rural social capital.

Nevertheless, it is also true that the negative image and performance of agricultural co-operatives in many LDCs and transition countries is still an existing problem and needs to be overcome. To overcome this negative image, there is an urgent need for governments to allow and even encourage greater autonomy of action of co-operative enterprises and to encourage the formation of other forms of producer group enterprises, such as *caisses populaires*, credit unions, producer unions and associations and small farmer groups.

In addition to the above, there is an urgent need to better inform governments and donors about the economic impact that successful co-operatives have in promoting local development. This will require an investment in serious quantitative research that assesses the economic impact of co-operatives on local development in terms of direct beneficiary household incomes, co-operative profitability and growth, broader indirect impacts on rural employment creation, on small business start-ups and on access to social services.

ANNEX

FAO Publications on Co-operative Development

Policy/issue papers

Developing Producer Groups and Rural Organisations in Central and Eastern Europe - Issues and Challenges, by John Millns, FAO Rome, May 2002. http://www.fao.org/waicent/faoinfo/sustdev/2003/PE0405_en.htm

Co-operatives: Has their Time Come – Or Gone?, by Michael Cracknell, FAO Rome, 1996.

Capital Formation in Agricultural Co-operatives in Developing Countries: Research Issues, Findings and Policy Implications for Co-operative and Donors, by JD Von Pischke, a paper prepared for International Technical Meeting on Capital Formation in Agricultural Co-operatives, Committee for the Promotion and Advancement of Co-operatives (COPAC), Rome, 8-10 November 1995.

Capital, Participation and Co-operative Performance; The Importance of Member Equity Stake by John Rouse, a paper prepared by FAO for IRMA Symposium Management of Rural Co-operatives, Anand, India, 7-11 December, 1992.

Planning of Programmes and Projects for the Promotion of Co-operatives and Rural Groups based on the AMSAC Concept (Appropriate Management Systems for Agricultural Co-operatives) FAO Rome, 1991

General information

Farmers' self-help organisations: Mobilising people's resources for development, brochure, FAO Rome, 1993.

*Guide pour la preparation de programmes et projets de promotion de co-operatives et groupements ruraux sur la base du concept GACOPEA gestion approprièe des co-operatives de petits

exploitants agricoles by Hans Munkner and Stefan Ruchius, FAO and DSE, Marburg, 1990.

Bi-annual Reports to COPAC on FAO activities in support of co-operative development FAO Rome, 1979-2005.

FAO and Agricultural Co-operatives Information Note by Ronald Gretton, FAO Rome, July 1967.

Guidelines, training manuals

New strategies for mobilising capital in agricultural co-operatives by J.D. Von Pischke and John Rouse, FAO Rome, 2004.

Computerizing Agricultural Co-operatives: practical guidelines by Roxana Bassi and John Rouse, FAO Rome, 2004.

Empowering rural producer organizations: guidelines, resource books and training manuals a CD-ROM, FAO, Rome 2004.

Mobilising capital in agricultural service co-operatives by John Rouse and JD Von Pischke, FAO, Rome 1997.

http://www.fao.org/sd/2003/IN0504_en.htm

Agricultural co-operative development: A manual for trainers FAO, Rome, 2002.

http://www.fao.org/sd/2003/IN07023_en.htm

Guide on Accounting Systems for Agricultural Co-operatives in Developing Countries in the Near East FAO, Rome (without date)

A Guide to Management of Small Farmers' Co-operatives by Gupta, VK and Gaikwad, VR, FAO Rome, 1983.

Case studies

Financing Economic Self-reliance and Member Participation in Farmer Organizations in Kenya by John Rouse in "Grassroots' Organizations, Decentralization and Rural Development: African Experiences in the 1990s," edited by Holmén, Hans and Luzzati, Enrico, International Training Centre of the ILO, Torino, 1999.

Capital formation in Kenyan farmer-owned co-operatives: a case study by

Jamsen, Pekka, Ikaheimo, Seppo and Malinen, Pasi, People's Participation Series, No.12, FAO Rome, 1999.

The Development of Independent Co-operatives in Zambia: A Case Study by Charles Chabala and Paul Ojermark, People's Participation Series, No.8, FAO Rome, 1994.

Re-orienting Co-operative Structures in Eastern Europe: Summary of Case Studies Central and Eastern European Agriculture in Transition Series No. 1, FAO Rome, 1994.

Re-orienting the Co-operative Structures in Selected Eastern European countries: Report on Workshop, Central and Eastern European Agriculture in Transition Series No. 2, FAO Rome, 1994.

Re-orienting the Co-operative Structure in Selected Eastern European Countries: case study on Former German Democratic Republic, Central and Eastern European Agriculture in Transition Series No. 3, FAO Rome, 1994.

Re-orienting the Co-operative Structure in Selected Eastern European countries: case study: Hungary, Central and Eastern European Agriculture in Transition Series No. 4, FAO Rome, 1994.

Re-orienting the Co-operative Structure in Selected Eastern European countries: case study on Poland, Central and Eastern European Agriculture in Transition Series No. 5, FAO Rome, 1994.

Strengthening and Developing Voluntary Farmers' Organizations in Eastern and Central Europe, Report on Workshop," Central and Eastern European Agriculture in Transition Series No. 6, FAO Rome, 1994.

Organisation and Management of Agricultural Services for Small Farmers of Eastern Europe, Central and Eastern European Agriculture in Transition Series No. 7, FAO Rome, 1994.

Notes

1 There were no credit unions in any of the CEE countries, but there were so called "savings and credit co-operatives" with a rather limited scope of activities subordinated to the state owned banking system. E.g. In Hungary, in practical terms they operated as a branch of the state-owned National Savings Bank. Even today, only in Poland there exists a new and quite strong credit union structure.

2 Holmen Hans, and Jirström Magnus, "The Challenge to Co-operatives as Tools for Development in Post-Structural Adjustment Africa" in Holmen and Luzzati, "Grassroots' Organisations, Decentralisation and Rural Development", International Training Center of ILO, Turin, 1999.

3 "Rural co-operatives as agents of change: a research report and a debate," Volume VIII in "Rural Co-operatives and Related Institutions as Agents of Planned Change," United Nations Research Institute on Social Development, Geneva, 1975.

4 Gow, David, et al, "Local organisations and rural development: A comparative reappraisal, 2 vols., Development Alternatives, Inc., Washington DC, 1979

Esman, Miltron and Uphoff, Norman, "Local Organisations: Intermediaries in rural development, Cornell University Press, Ithaca, New York, 1984

5 Mobilizing capital in agricultural service co-operatives, FAO, 1997, page 5.

6 Agricultural Co-operative Development – A Manual for Trainers, FAO, Rome, 2002

7 "Farmer organisations in central and Eastern European countries and their role in the provision of input-output services in the context of accession to the European Union" in John Millns:"Participatory Farmer Group Development – Experiences from the Balkans", FAO, Rome 2005

8 Research with Government of Finland support and assistance from international experts, J.D. Von Pischke and Michael Cook

9 Von Pischke, J.D. and Rouse, J.G., "New strategies for mobilizing capital in agricultural co-operatives," FAO Rome, 2004.

10 Ibid.

11 *Computerising Agricultural Co-operatives: practical guidelines* by Roxana Bassi and John Rouse, FAO Rome, 2004.

JOHN MILLNS

DEVELOPING AGRICULTURAL CO-OPERATIVES AND PRODUCER ORGANISATIONS IN MALTA – ISSUES AND CHALLENGES

Summary

Agricultural co-operatives were first established in Malta as early as 1947 and most survive today. They should have a central role to play in enabling their members to take an active part in exploiting new economic and social challenges. Malta is now a member of a trading block that has more than 400 million consumers and since joining the European Union (1 May 2004) the environment within which Maltese farmers, rural communities and agricultural co-operatives now operate has changed and there are a number of new comparative advantages and potential opportunities for the innovative to exploit.

However Maltese farmers and their co-operatives often perceive weaknesses and threats to their sector, rather than new opportunities and a major concern is that many farmers will simply abandon production. Between 1999 and 2004, total sales turnover of Maltese agricultural co-operatives fell by 19%, and surpluses by 62%. For many Maltese agricultural co-operatives it seems that they still need time to mobilise their resources, build on their strengths and managerial capacities and learn to cope with the pressures

of competitive markets and increasing independence from the State.

A policy environment needs to be created that further enables Maltese co-operatives to:

- Be dynamic, flexible and market led
- Provide measurable benefits to the farmer members that use the group
- Have a well trained, motivated and visionary management
- Establish and implement long term plans and strategies
- Make quality and added value improvements
- Have further independence and autonomy from the Government and be directed by the users – farmers

Farmers, their co-operatives, the APEX, Government and support service providers all have a role to play in creating such an environment.

The *Government* will need to continue to maintain and communicate clearly defined agriculture and rural development policies and present a vision that will help Maltese agriculture to become more efficient and competitive, and generally encourage and promote a culture across the agri-rural sector of consultation, local decision-making, group enterprise, innovation and team building. Further autonomy could be given to the agricultural co-operative sector through removing all direct investments and shareholdings into co-operative assets and any influence on decisions at co-operative board level and ensuring that the Co-operative Board focus only on regulatory and monitoring activities. Assistance could be provided by contributing to commodity discussion groups, providing up to date and relevant information on EU and national development initiatives, sub-contracting the management of research, information and training to private enterprise and continuing to provide part finance for implementation.

If Maltese *co-operatives* are to capitalise on the positive aspects of change they must develop appropriate structures and procedures. They will need to prepare and implement 3-5 year plans that focus on the commercial aspects of member activity and avoid crisis management, political debate or philosophical arguments. The unique sales points of Maltese production needs to be better promoted, innovative products and systematic sales strategies developed and electronic and information technologies better exploited. Linkages, agency and finance agreements with processors, retailers and exporters can be improved, commodity focused producer organisations strengthened and strategic alliances and cooperation improved between co-operatives. Most importantly their further development will depend on a committed and active farmer membership.

Both the Co-operative Fund and the APEX organisation can provide support through enabling specific initiatives that will support agriculture and rural development. The APEX in particular needs to establish credibility by presenting a clear strategic vision, preparing a detailed business plan, employing full time management, strengthening the financial base and providing specific consultancy, advice, research, information and policy support services.

This paper presents ideas on how this may be achieved and is intended to stimulate further discussion and debate.

1. Agricultural Co-operation in Malta

Since joining the European Union on 1st May 2004 the environment within which farmers, rural communities and agricultural co-operatives in Malta now operate has changed. The European Union has influenced agricultural policymaking and Maltese producers, traders and processors are now faced with increased import competition, the realities of a common agricultural policy and new trading regulations and standards. Since May 2004 most import levies, duties and excise taxes with EU partners have been dismantled. Malta and Gozo is now a member of a trading block that has more than 400 million consumers.

The country has a number of comparative advantages and potential opportunities when compared to other EU member countries. Its geographical position allows export possibilities into the EU to be further explored as well as with Arabic and North African markets. New products can be developed for niche markets and new varieties and breeds introduced in order to better exploit the most southerly Mediterranean climate in the EU. Malta is also one of the most densely populated countries in Europe and the population further swells in the summer time with an influx of tourists. The country has a well-educated population and a relatively high GDP per head and particularly when compared to recent accession countries from Central and Eastern Europe. A large percentage of the population are able to speak fluent English as well as many other European languages.

Although agriculture employs less than 2% of the population, and contributes a similar amount to the GDP, farmers still manage more than 80% of Maltese land and directly and indirectly they can affect tourism (and a variety of other business sectors), the environment and the quality of life for the majority of the population. While land ownership is accepted as a right, farmers are also generally perceived, amongst the wider population, to have a duty of stewardship and yet compared to other business sectors, Maltese agriculture has encountered particularly strong competition following EU membership and in recent years a decline in incomes.

The Government has negotiated with the EU a number of agreements that enables direct income support to be provided to farmers as a replacement to levies and financial support to be provided for the restructuring of the agri-processing industry and equivalent to a financial package of €184 million over the next decade. Much of Malta and the whole of Gozo are also designated by the EU as a less favoured area and this enables additional compensatory payments to be made as well as enabling access to regional development funds.

However more often Maltese farmers perceive the weaknesses and threats to their sector, rather than the new opportunities and a major concern remains that many farmers over the next few years will simply abandon production. Agriculture employs only 1.84% of the population of Malta and this is declining. The sector faces major structural constraints posed mainly by land and water scarcity and relatively high labour and other input costs. Most production is from small and intensively cultivated plots and the only significant agricultural export is potatoes. Local produce accounts for only one third of food consumption and the remainder is met by imports.

To improve competitiveness as well, as to meet EU imposed standards, a major priority for the Government is to help in modernising farms and improving efficiency, (such as by encouraging the increasing adoption of plastic tunnels and drip irrigation) as well as to improve agri-marketing, distribution and processing. This will take time and money and, in theory at least, producer co-operatives and rural organisations should have a central role to play in enabling their members, to take an active part in exploiting new economic and social challenges. The Government is seemingly aware of the need for viable farmers co-operatives. The Constitution of Malta proclaims that, "the State recognises the social functions of co-operatives and shall encourage their development". The Co-operative Societies Ordinance was enacted in 1946 and the first agricultural co-operatives in Malta were registered in 1947.

Currently there are more that 55 registered co-operatives and operating in practically all sectors of the Maltese economy (although there are no retail or housing co-operatives). 17 agricultural co-operatives represent 90% of the co-operative sector by both financial turnover and membership but they do vary significantly in terms of market share and size. Five agricultural co-operatives (primarily poultry) have had hardly any sales turnover at all for more than 5 years. Another five contribute more than 95% of total agricultural co-operative sales turnover and surpluses. These are the Pig Breeders Co-operative Society Ltd (5,814,732[1]), the Milk Producers Co-operative Ltd (5,816,105 LM) the Farmers Central Co-operative Society Ltd (1,480,083 LM), Koperattiva Ghawdxija Agrikola Gozitano Ltd (845,461 LM) and the Agri-Coop Ltd (848,834 LM).

Overall debt to equity levels are relatively low in Maltese agricultural co-operatives, however total sales turnover fell by 19%, and surpluses by 62%, between 1999 and 2004, and both continue to fall. Detailed statistics on individual co-operative turnovers and surpluses is shown in table 1 below.

Co-operatives in Malta have been seen as having a social as well as commercial responsibility and since their formation agricultural co-operatives have been regulated by various Ministries and including Agriculture and Fisheries, Education and Social Policies. A Co-operative Board regulates, licenses and monitors co-operatives on behalf of the Government and also provides training, information and website support facilities. Co-operatives pay no commercial tax but do pay a compulsory 5% levy on surpluses into a co-operative fund and to be used in further strengthening and developing the sector. Until recently co-operative members paying social security contributions, through their co-operatives, were also able to obtain additional rebates from the Government. Some sectors were also largely protected from liberalised trade, through prohibitive tariffs on imports, quotas and compulsory co-operative membership.

Healthy co-operative business development and direct political interference seldom go together and in recent years the Government has gradually allowed existing co-operatives greater freedom over managing their own affairs, but even today their involvement in cooperation still includes part ownership, finance and even management. Co-operatives should not have to rely on Government to stimulate their growth, but in Malta they still need further independence and autonomy from the State and time to mobilise their resources, build on their strengths and managerial capacities and learn to cope with the pressures of competitive markets.

In 2003 the EU noted, in the official Maltese progress towards accession report, that, "insufficient progress for the introduction of a legal framework and administrative structures for the establishment of common market organisations, including the activities of producers and

Table 1 Agricultural Co-operative Turnover and Surplus Statistics 1999 – 2004 (Data provided by the Co-operative Board of Malta)

Name of Cooperative (Date of Registration)		1999
Pig Breeders Co-operative Society Ltd (1983)	T	8,722,587
	S	97,207
Milk Producers Co-operative Ltd (1958)	T	6,035,884
	S	594,379
Farmers Central Co-operative Society Ltd	T	1,620,154
	S	24,600
Koperattiva Ghawdxija Agrikola Gozitano Ltd (1959)	T	836,530
	S	26,300
Mgarr Farmers Co-operative Society Ltd (1947)	T	192,760
	S	9,509
Rabat Farmers Co-operative Society Ltd (1947)	T	113,685
	S	(5,024)
Siggiewi Farmers Co-operative Society Ltd (1947)	T	71,509
	S	218
Farmers Wine Co-operative Society Ltd (1960)	T	42,969
	S	5,289
Qormi Farmers Co-operative Society Ltd (1947)	T	35,325
	S	77
Zabbar Farmers Co-operative Society Ltd (1947)	T	53,096
	S	154
Dingli Farmers Co-operative Society Ltd (1947)	T	21,729
	S	1,090
St Paul's Bay Farmers Co-operative Society Ltd (1947)	T	13,030
	S	(590)
Koperattiva tat-Tjur Limitata (1997)	T	(1,211)
	S	Nil
Koperattiva Ghawdxija tas-Serer Limitata (2001)	T	N/A
	S	N/A
Koperattiva Ghawdxija tat-Tjur Limitata (2002)	T	N/A
	S	N/A
Broiler Breeders Co-operative Ltd (2002)	T	N/A
	S	N/A
Koperattiva Ghawdxija Produtturi tal-Gbejniet Ltd. (2003)	T	N/A
	S	N/A
Agricoop Ltd.	T	861,784
	S	22,461
Total Turnover (Lm)		**18,619,831**
Total Surplus (Lm)[2]		**775,670**

2000	2001	2002	2003	2004
8,352,842	8,582,638	8,571,955	6,759,403	5,814,732
79,353	93,720	68,973	63,617	68,576
5,789,181	6,079,736	6,128,352	5,741,138	5,816,105
248,162	429,913	494,940	525,076	246,601
1,545,842	1,579,524	1,618,591	1,655,971	1,480,083
12,094	4,730	(24,512)	11,891	(16,760)
682,705	726,933	1,005,058	1,005,157	845,461
30,054	22,775	41,938	30,037	15,704
203,735	214,375	224,616	222,138	205,345
11,220	10,224	12,966	3,446	6,899
111,874	101,165	90,801	78,541	N/A
(5,986)	(6,439)	(10,340)	(18,057)	N/A
61,831	82,063	76,353	83,287	70,515
265	(192)	(185)	(181)	(178)
39,608	42,420	43,456	36,914	29,830
5,542	4,574	4,746	2,115	477
25,172	30,003	34,837	34,128	35,793
77	(135)	(135)	(135)	(135)
57,340	37,283	28,704	33,553	2,531
682	447	(623)	(1,004)	(936)
19,227	20,198	16,304	28,902	20,903
1,086	1,146	1,146	1,146	1,132
17,227	11,156	9,646	4,892	6,566
375	458	231	161	189
(1,559)	(1,950)	(3,784)	N/A	(a)
Nil	Nil	Nil	Nil	(a)
N/A	Nil	500	0	N/A
N/A	(561)	225	(59)	N/A
N/A	N/A	N/A	N/A	N/A
N/A	(359)	23	N/A	N/A
N/A	N/A	N/A	N/A	N/A
N/A	N/A	N/A	N/A	N/A
N/A	N/A	N/A	N/A	N/A
N/A	N/A	N/A	N/A	N/A
869,807	885,938	891,772	894,796	848,834
52,553	33,717	16,619	28,874	(25,593)
17,774,832	**18,391,482**	**18,737,161**	**16,578,820**	**15,176,698**
435,477	**594,018**	**606,012**	**646,927**	**295,976**

processors organisations had been made". The Minister for Rural Affairs and the Environment for Malta, during the 5th APS Bank annual seminar on the development of agriculture and fisheries in Malta, outlined the position of agricultural co-operatives in Malta as being in a state of transformation and emphasised that "the economic, social, and legal environment of co-operatives are changing and requiring adaptive measures. The withdrawal of government control from the market, public policy, international trade liberalisation and expansion, new technological developments, changing consumer demand, concentration and integration processes in product and marketing chains are but a few examples, yet all of them have a huge impact on the development of Maltese co-operatives, placing them under great pressure to adapt themselves to new realities".

Since then the Government has been committed to pursuing an agricultural co-operative business development programme that has been primarily focused on setting up new producers organisations[3]. Initially this was as a pre-accession measure and is now a programming measure within the Rural Development Plan for the Maltese Islands 2004 - 2006. If grant support is to be provided to producer organisations, the European Union expects specific guidelines, to be followed in relation to membership numbers, product commitment, member only trade, organisational structure and their degree of market influence. Few existing Maltese co-operatives meet the necessary criteria, although recently Koperattiva Ghawdxija Agrikola Gozitano Ltd has been approved for fruit and vegetable production and marketing and three new groups have been formed, one for export of potatoes and two for tomato processing.

However it is important that groups are not simply viewed by producers, advisers or policy makers as a way of supporting inefficient and non-viable farms or other rural businesses or as a miracle cure for all the problems that beset rural areas. During February 2005 the Food and Agriculture Organisation of the United Nations conducted a survey with the farmer boards from ten Maltese Agricultural Co-operatives[4]. Each board was asked to present key issues affecting agricultural co-operatives as well as to assess their strengths and weaknesses as well as opportunities for their future development and threats to their existence. Almost sixty key issues were raised by farmer directors (top 20 presented as table 2). More than two thirds cited problems at farm enterprise level and including small land plots, part time and ageing farmers, low numbers of livestock per farmer, low levels of mechanisation, high and increasing production costs and a need for further farm restructuring and improved land access. More than half were concerned with increasing imports, and made references to, increasing buyer preferences for imported products, the increasing numbers of importers, the legality of imports, the low level of inspection on quality and traceability, as well as a general lack of Maltese competitiveness compared to imported production.

Meetings were held by FAO with farmer directors and representatives and some generic issues were identified in relation to production and marketing:

In relation to *production* the main opportunities were generally perceived as being, for co-operatives to help members to improve overall standards on farms, to reduce farming costs and to use existing property and equipment on farms more effectively and specifically in relation to:

- Harvesting earlier and better exploiting early crop possibilities from a southern Mediterranean climate
- Introducing new product varieties, further specialising in high value production and improving genetics through natural selection and AI (livestock)

Table 2 Key issues influencing agricultural co-operative development in Malta – Perceptions of farmer directors of Maltese agricultural cooperatives
(The % indicates the number of directors ranking the issue within their top 5 priorities)

Rank	Issue	%
1	Problems at farm enterprise level	67%
2	Increasing importation of product	58%
3	Planning authority (MEPA) regulations	44%
4	Input costs (fertilisers/equipment/young stock/feed/fuel costs/electricity)	42%
5	A lack of farmer cooperation across the agricultural sector and including a lack of member loyalty, trust or cooperation between cooperatives	40%
6	Low financial returns and product prices, declining incomes and an uncertainty on whether to invest in the long term	33%
7	Insufficient technical support and advisory services and information	29%
8	The role of new forms of EU supported producer organisations	29%
9	SMPPMA[5] issues and a lack of financial suitable incentives and subsidies	27%
10	A lack of cooperatively owned added value activity (such as for grading, packing, storage or processing)	25%
11	Poor marketing	20%
12	Poor product traceability and quality certification (local and import)	18%
13	Illegal activities and a lack of controls and inspections	18%
14	Unfair (non-cooperative) competition and a general opposition to cooperation from Government and traders	14%
15	Government bureaucracy and too many new regulations introduced in a short time	14%
16	A lack of export activity or exploitation of EU markets	14%
17	The Government not using the EU safeguard clause to protect local production	13%
18	The distance from markets and transport between islands[6]	13%
19	Waste management directives and farm waste issues	11%
20	A lack of adequate finance and investment for development	11%

- Further standardising, guiding and controlling production from member farms to reduce over-production and improve marketing
- Producing more EU subsidised and protected crops, such as olives and grapes
- Further sourcing and importing, through their co-operatives, quality raw materials (such as fodder, equipment, livestock and feeds), out of season and organic production and production not in competition with local production
- Considering more often the environmental implications of agriculture, through further encouraging the use of natural fertilisers and making better use of waste and providing recycled effluent water
- Conducting more livestock and crop research in association with research institutes

In relation to *marketing* the main opportunities were generally perceived as being, for co-operatives to better identify buyer and consumer needs, add value, and promote the freshness and quality of Maltese production in both local and export markets. Specific opportunities were presented in relation to:

- Improved research into domestic and export markets
- Developing, for specific products, Maltese, regional and product brands, logos and recipes
- Developing niche markets, in Malta and overseas, such as for organic or semi-organic production
- Better promoting and advertising hand picked Mediterranean brands and the taste and health aspects of Maltese production
- Focusing on improving quality specifications, standards, labelling, marking, traceability and certification of all production

- Improving the presentation of products through better grading and packaging
- Employing more sales people
- Specifically targeting retail and food catering buyers
- Developing weekly farmers markets and promoting farm gate sales
- Better exploiting export opportunities that are available in EU markets
- Better educating Maltese consumers on Maltese production

In Malta there is no shortage of institutions able, and willing, to support agricultural co-operatives. The APS Bank is particularly active in promoting and investing in the agriculture and co-operative sector. The Agricultural Institute at the University of Malta provides research, policy and advisory services and education programmes in agriculture. MCAST is an agricultural vocational training institute offering Higher National Diploma (HND) courses. A Government research centre focusing on livestock production exists in Malta and for fruit and vegetable production on Gozo. The SCOOPs programme promotes cooperation in schools and the Outlook and MediaCoop consultancy companies provide specialist advice for co-operative enterprise development. However the APEX organisation is the only organisation in Malta specifically owned, and partly directed by, farmers through their co-operatives[7].

The APEX is a representative body for both agricultural and non-agricultural co-operatives[8] and has operated informally in Malta since 1978. It was registered as a legal entity in 1990. In recent years the APEX has attempted to develop its national activities and to link with pan-European bodies, such as COPA/Cogeca and the International Co-operative Alliance (ICA). Even so the services offered by the APEX are very limited and in recent years the organisation has had little real influence in developing agricultural policy and its services have largely been limited to organising meetings, visits and providing information to co-operative members.

2. Opportunities for strengthening the organisational and business capacities of agricultural co-operatives in Malta

Few producers are individually large enough to make significant impacts on national and global markets. Across Europe today agricultural co-operatives trade more than half of inputs that are supplied to, and the produce marketed from, farms. Farmers direct some of the largest agri-business trading, finance and insurance businesses in Europe. Most have started from relatively modest beginnings and have grown with little direct Government or donor support.

In Malta co-operatives have a significant market position in the supply of inputs and marketing of dairy, fruit and vegetables, fish and pork but in few other agricultural sectors. In recent years sales turnover has declined and margins tightened for most co-operatives and if they are to capitalise on the positive aspects of change they will need to be dynamic, flexible, optimistic, and develop structures, standards and procedures over time that are in response to changes in the commercial, political and social environment. Farmers, their co-operatives, the APEX, Government and support service providers all have a role to play in creating an environment in which enables Maltese agricultural co-operatives to:

- Be dynamic, flexible, market led and commercially competitive
- Have a committed and active membership and to provide measurable benefits to those that use their services
- Have a well trained, motivated and visionary management
- Establish and implement long term plans and strategies and to avoid crisis management
- Make quality and added value improvements
- Be directed by the users – farmers
- Be depoliticised and have further independence and autonomy from the Government

2.1 The Role of the Government, the Co-operative Board and the Co-operative Fund

The problems and opportunities currently facing agricultural co-operatives in Malta have partly resulted, not only from Government policies towards agricultural co-operative development, but also from the influence of broader national agricultural policies and issues at farm enterprise level. In particular joining the European Union in May 2004 has significantly influenced the thinking of Government and the future of agriculture. However while the Common Agricultural Policy constrains the Governments ability to make unilateral decisions it also provides new opportunities for the innovative to exploit.

The Government needs to continue to maintain and communicate clearly defined agriculture and rural development policies that will help Maltese agriculture to become more efficient and competitive and to be both economically and environmentally sustainable. In particular there is a need to maintain strategies that will assist or ensure:

- Increases in farm size and land access and the numbers of commercial and full time farming enterprises
- The development of innovative, competitive and profitable enterprises and products
- The increasing introduction of appropriate production, communication and marketing technologies and innovations
- The adding of value, the development of different and unique sales propositions, the improvement of brand recognition and marketing and the exploitation of the strengths of Maltese production
- Improved vertical integration and commercial linkages
- Proper management of environmental resources and rural areas
- Increased investments into agriculture and rural development
- The availability of relevant research, information, training and advice on EU and national policies and programmes
- Fair and legal competition
- A reduction in unnecessary bureaucracy, legislation or administration

Assuming these policies are in place agricultural co-operatives should need no special exemptions when compared to other forms of private enterprise. However if Maltese farmers are to take greater responsibility for developing and managing their groups there are a number of issues that need to be addressed.

Co-operatives maintain a significant position in Maltese agriculture, unlike any other business sector and they dominate or significantly influence production and markets in the dairy, pork, beef, fruit and vegetable and input supply sectors. But despite this responsibility for supporting or encouraging co-operative development is retained by the Ministry of Education. The Ministry for the Environment and Rural Development deals with (individual) agricultural co-operatives by direct contact through a number of departments including:

- The Offices of the Minister of Agriculture, Permanent and Parliamentary Secretaries
- Advisers from the Agricultural Services and Rural Development Division
- Advisers and inspectors from the Agricultural Research and Development Centres
- Veterinary and Crop Inspection Officers
- Agri-Policy Development Advisers

Each has its own role with the Ministry hierarchy and this has sometimes resulted in co-operatives receiving conflicting, confusing or inaccurate advice and largely as a result of individual interpretation rather than as a result of Government or EU policy.

Currently the main focus for farmer group development within the Government has been primarily focused on setting up new producers organisations and as a programming measure within the Rural Development Plan. The terms producer organisation and co-operative are often referred to as separate forms of organisation in Malta, although in reality both should be aiming to achieve the same objective i.e. to maximise benefits to farmer members that use the group and its services. This seems to still reflect a broader and generally underlying perception amongst the authorities, and many Maltese farmers, that co-operatives are not really controlled by farmers or solely represent member interests and that producer organisations need to be established to access EU grants.

Despite transferring a lot of control over the past decade, the historical legacy of the Government in influencing the establishment, control and management of many agricultural co-operatives still influences the thinking of many officials, farmers and co-operative managers. In the current economic environment, and if the more established co-operatives are really to exploit competitive opportunities, the Government will need to further re-structure its relations with the agri-co-operative sector and in particular to enable their even greater autonomy. There is a now no need for Government direct investments and shareholdings into co-operative assets or for them to influence decisions at co-operative board level, second staff, or to sit on the boards of co-operative representative bodies.

If, in principle, further autonomy for the co-operative sector is accepted then the role and responsibilities of the Co-operative Board and the Co-operative Fund will also need to be reviewed. The primary responsibility of the Co-operative Board is to register co-operatives, ensure they are conforming to the provisions of the law, investigate and penalise illegal activity and liquidate non-conforming or insolvent operations. It is however questionable as to whether the Board should continue to carry out activities that could be equally provided by the private sector, such as co-operative education, research, promotion, training or consultancy activities.

Further autonomy does not mean the Government divesting itself of all responsibility or interest in cooperation. Indeed a healthy and sustainable co-operative sector in agriculture should substantially help farmers and the wider rural community to develop their own initiatives, to stimulate innovation, to improve communication and to promote trade. With EU support the Maltese Government is already promoting the development of producer groups for specific sectors. Other EU programmes such as Leader similarly attempt to encourage “bottom up” initiatives of local groups in all areas of local and regional enterprise and social development. Most EU structural funds, or funds available for less favoured areas, place widespread local stakeholder consultation at the core of their development initiatives and encourage cooperation between primary beneficiaries. The aim is not only to establish and develop co-operatives but also to encourage a wider culture of consultation, local decision-making, group enterprise, innovation and team building.

In Malta commodity groups, involving farmers, traders, processors, retailers and consumers would also help the consultation process, exchange of information, integration of the sector and help in tackling key issues. Adopting such an approach would require a long-term vision to be supported by series of targeted, information, research, training and development initiatives. The Government need not necessarily provide these themselves but can sub-contract management responsibilities to private enterprise (co-operative and non-co-operative) for defined projects and programmes, either by matching or part funding (based on the proposed level of own stakeholder contribution) or by enabling full funding and by preparing detailed project terms of reference (TORs) and inviting competitive tendering. Budgets and department project responsibilities would need to be allocated to enable project tendering, monitoring and audit and the Co-operative Board could have a role to play in this regard.

The Co-operative Fund could also provide a useful impetus for many relevant programmes. However despite having accumulated reserves in excess of 1 million USD its initiatives in recent years have had little impact in helping to stem the decline in agricultural co-operative turnover and surplus or to tackle many of the key issues influencing agricultural co-operative development in Malta and as perceived by farmer directors of Maltese agricultural co-operatives (Table 2).

The Government maintains influence on the Board of the fund and under the premise that co-operatives pay no commercial tax but contribute a compulsory 5% levy on surpluses into the fund. However such an arrangement neither contributes to the Government budget nor truly enables independent fund management by the co-operative sector.

Agricultural co-operatives contribute more than 90% of the income to the fund and while other co-operative business sectors are continuing to be established, and are growing, agricultural co-operatives continue to decline. There is a specific need for at least a proportion of the Co-operative Fund to be allocated to helping to tackle the many modern day key issues not just for agriculture but also for rural development.

2.2 The Role of Farmers, Agricultural Co-operatives and the APEX

The main challenge for Maltese agricultural co-operatives today is to help in developing a competitive agricultural sector and to provide support services that are arranged to fit the complexities of new realities. Co-operatives should have an important role to play in providing the necessary information, organisation, training and support to enable their farmer members to make informed decisions, improve their productivity and competitiveness and take a more active role in market development.

There is a need to further enable and motivate farmers to lead and develop their co-operatives, to create a positive atmosphere (within which opportunities can be exploited), to establish and communicate 3-5 year plans with clear objectives and strategies, and to avoid crisis management. Yet few (if any) Maltese agricultural co-operatives have prepared effectively for EU accession and most still do not have a clear strategic vision and a detailed plan as to how they will develop their business. Many farmers in Malta still see their own co-operatives as political pressure groups lobbying for more protection through the government, rather than as genuine, voluntary, self-help business organisations directed by farmers and providing them with the necessary services needed for to increase value-added production and for the achieving economies of scale in the market place.

Agricultural co-operatives need to avoid philosophical arguments and not become unnecessarily overburdened with inappropriate dogma. Most farmers join co-operatives because they can reduce their costs, increase the prices received for their production or help to spread their risks and like all other private enterprises, they require proper finance, planning, market, economic and environmental analyses, good third party relationships and well-trained, motivated and visionary management. Most importantly their development depends on a committed and active membership and the willingness of farmers to plan, develop and continually improve their own jointly organised activities and provide measurable benefits to their members.

Maltese agricultural co-operatives can become more commercially competitive. However costs will need to be assessed to see how savings can be made and profitability improved. Markets will need to be better analysed to identify buyers and consumer demands and sales strategies implemented which are focused on contacting, keeping and developing the customer base and exploiting the unique sale points of Maltese production. To obtain higher incomes they will need to identify those buyers that are prepared to pay higher prices for agreed standards of produce quality, quantity and delivery reliability and present them with innovative and competitive products and services. Co-operatives can also better exploit opportunities presented by new and innovative electronic and information technologies. Added value activity can be developed or diversification considered with cooperation into other business sectors (such as exploiting tourist possibilities) and activities can be further integrated vertically by improving linkages and agency agreements with existing buyers (processors, retailers and exporters).

Finance can be improved by focusing on more profitable activity, retaining surpluses, seeking improved credit and payment terms from buyers and banks or developing advanced credit schemes with input suppliers and traders. Many agricultural co-operatives still manage with low financial gearing and so potentially could obtain loan capital for specifically defined and planned business opportunities.

Co-operatives can avoid conflicts between each other by regularly discussing and exchanging information on production, marketing, technical, financial and management issues. They can merge or develop strategic alliances together or with foreign co-operative partners. They can even help to support and strengthen commodity focused producer organisations either by organising themselves as a producer organisation (such as the Koperattiva Ghawdxija Agrikola Gozitano Ltd) or by encouraging their establishment and acting as a management agent.

Such approaches may help Maltese agricultural co-operatives to find new ways of strengthening "active" membership, encouraging young farmer activity, better exploiting the value of a member base and improving member loyalty, discipline and commitment. A number of other possibilities exist, such as by simplifying rules and procedures, introducing payments based on produce commitment and quality improvements, discouraging trade with non-members, enforcing standards for production and marketing, presenting full financial and management transparency or simply focusing services on member issues and concerns and improving member communications, links and networks. Each co-operative will have to carry out a situation analysis on their own terms, trace their own path and generate their own innovations.

On-going changes in the agribusiness environment in Malta is requiring farmers to upgrade technologies, acquire new technical skills and their co-operatives to adopt different approaches to management. This can be inhibited not only by insufficient support institutions and information, but also by inappropriate management capacity and knowledge. For many co-operatives a lack of entrepreneurial ability and management skills often play a bigger role than capital constraints. Malta being a relatively small island and business sector enables rapid exchange of information and ideas but also limits the human resource base and instils prejudice and sometimes complacency.

It is important for co-operatives to employ competent executive management, and this includes competitively remunerating farmer directors and management. Farmer boards need to have relevant and complementary skills and have mechanisms for encouraging new blood to be brought into management committees. Consideration can also be given to exchanging and seconding farmer directors (not legally possible in Malta at the present time) and managers between co-operatives, or introducing non-executive, non-voting board members as advisers from other business sectors (co-operative and non-co-operative), in areas such as for planning or finance. Non-executive board directors or managers might also be recruited from outside of Malta.

All this can be facilitated by well targeted, structured and certified advisory, training and information support. Basic and advanced vocational training needs to be available to producers who wish to improve their expertise in business management, technology or new production processes or to be retrained in new vocational skills if they intend to leave farming. Farmer directors and prospective directors would benefit from short courses covering their roles and responsibilities, business planning and marketing, meeting and decision-making skills, member communications and understanding of finance.

However if a co-operative is to be really assisted, the aim must be to facilitate reflection by the group itself. The process of co-operative development is strengthened when farmers themselves begin to assess the importance of a problem and whether it can be solved. There is a need to deliver relevant, practical and participatory training and advisory approaches to farmers at co-operative board level, to further stimulate teamwork and to focus on leading and visionary farmers that are capable of driving ideas forward as well as being able to communicate effectively with other producers, buyers and suppliers.

Potentially the APEX organisation has a significant role to play in stimulating change, development and growth in the agricultural co-operative sector. However at present it is significantly restrained by the lack of a clear strategic vision, full time management or proper control over its own finances. It is largely dependant on the voluntary initiatives of individual board members or their co-operatives. It is 100% financed through the Co-operative Fund and currently not presenting, or implementing, specific initiatives that will really help to tackle the important agricultural cooperation or agricultural policy issues in Malta. As a result it is not well recognised by the agricultural authorities, (which prefer to work directly with individual farmers or co-operatives), defended by farmers or being actively strengthened by their co-operatives.

If member co-operatives are to better use and exploit membership of the APEX the organisation has to strengthen its financial base away from a single dependency on the Co-operative Fund (such as by charging for specific consultancy, training, legal, audit, technical, banking, insurance or other services or by tendering for EU or national service or technical assistance contracts). It will also need to convince its members that they are directly paying a membership "fee" for which they obtain defined benefits. If agricultural co-operatives are to be convinced, specific initiatives will have to be developed that will help to tackle current agricultural and rural development issues.

Most farmers will expect the APEX to further lobby Government for enforcement of the law and particularly in relation to imported production and to help them to get further financial support and subsidies through the SMPPMA and other programmes. Certainly the APEX should work with, and be consulted by, the Government in these areas but potentially it also has the possibility to offer a much broader range of services.

The APEX has already assisted in establishing relations with COPA/Cogeca[9] and now has a direct representation. A strengthened agribusiness focus within the APEX would also better enable specific commodity groups to be formed. These groups would be able to tackle specific issues, through improved information collection and dissemination, facilitation of meetings to stimulate debate, innovation and decision-making and enable representation on stakeholder groups, involving Government, buyers and consumers.

The APEX could also assist individual groups to develop strategic plans, through facilitating the process and providing background research as well as encouraging intra co-operative trading. They could also be more closely involved in helping to design of national and pan European agribusiness research and training programmes and networks by improving or strengthening links with relevant training, advisory and research institutes and specialists, Ministry departments and the Chamber of Commerce.

The APEX could help in exposing members to new technologies and disseminating experience from national and European trials and research or in identifying programmes and disseminate information (in Maltese) on EU agri-support and regional development initiatives. They could help to improve the technical and business education of farmer members by, contracting specific Maltese or international training and advisory expertise, organising visits to foreign co-operatives and exchanges of farmer directors and managers, encouraging co-operative premises to be used as educational support facilities, helping to provide training incentives to young farmers and developing vocational training accreditation programmes with organisations such as MCAST

Table 3 Imports of Poultry Meat into Malta 2002-2004
Source: National Statistics Office,
Agriculture and Fisheries Unit

	2004	2003	2002
Value LM	3,563,442	871,906	566,099
Qty Kg	2,876,060	917,853	595,053

Case Study: The Poultry Sector in Malta – Development and Co-operation

John Millns and Egon Samler

The Food and Agriculture Organisation of the United Nations (FAO) were requested by the Maltese Ministry of Rural Affairs and the Environment to take a particular review of the poultry co-operative sector[10] and particularly as poultry production and marketing in Malta is highly fragmented when compared to dairy and not vertically integrated and poultry meat imports have also risen by more than 700% since 2002 (Table 3)[11].

Poultry slaughtering also dropped by 17% from 2003 to 2004. It is perhaps surprising that Maltese consumers are increasingly buying imported frozen poultry meat rather than the local fresh product, which is only on average 10% higher in price and of better standard. The current trend in most developed countries is a shift from frozen to fresh poultry meat. Maltese producers and processors argue that thawed poultry meat is being old fresh (a highly dangerous practice) but this is relatively easy to spot and against health laws. Certainly the broiler sector has a potential to further exploit the fresh market. At present frozen poultry meat imports are 36% (3,560 tonnes) of the total market and local fresh meat production 64% (6,300 tonnes). Across Europe the fresh poultry meat consumption represents more than 80% of the market suggesting a potential for local production to reach at least 8,000 tonnes i.e. an increase of 27%.

An EU compensation package has been agreed for poultry (€11 million) and eggs (€14.5million) and since joining the European Union this has been administered both as a direct payment and as aid for restructuring and will continue until 2010. Producers receive €15 per kilo subsidy of which €5 is allocated for upgrading of the sector. Malta also negotiated a three-year period of transition to EU welfare standards for laying hens and primarily related to cage height and floor slope. Even so poultry producers and processors continue to lobby for further financial support from the Government

However other issues also need to be considered. Average grower costs are estimated at 39.0 ¢/kg and income for a broiler grower is 43¢/kg with payments sometimes delayed by up to 8 months. Growers receive a subsidy of about 4¢/kg for the first 1.3 kg produced. Maltese farmers are only allowed to grow five batches per year at a stocking density of 13 birds per sq metre, primarily because the amount of subsidy per kg is calculated on this basis and at a 1.3 kg live weight.

Broiler houses on the Maltese islands have a different look to those usually found in other parts of the world. They are high, narrow and short. This makes them less efficient in regards to management (ex. heating and ventilation) and even increases the production cost. Most of the buildings are naturally ventilated or have fan-assisted ventilation. This can be a serious problem especially in summer when temperatures are reaching 35°C and with humidity over 70%. In such cases (one or two batches per year) the only reasonable solution would be the use of tunnel ventilation system that is based on high air velocity (2.5m per second at the chicken level) and the use of evaporative pad coolers.

Growers are rearing mainly two types of breeds, the Ross 308 and Hubbard and which they buy from the three hatcheries found in Malta. Two of the hatchers have both a hatchery and a slaughterhouse The chicks are bought as day-old chicks[12] originating from imported hatching eggs (two hatcheries) and a parent stock (one hatchery).

Sometimes the day-old chicks brought to the farm are not uniform in size and sometimes the weight of some chicks is smaller than the minimum standard (34 grams originating from hatching eggs of 52 grams). As a result of the lack of uniformity the grower has a higher than normal mortality rate in the first days. The lack of uniformity influences not only the mortality but also the final weight of the slaughtering bird. Due to instable demand for chicks it is difficult to keep a parent stock farm on the island but keeping a larger parent stock would make it easier to control the chick standard of the chicks.

Some farmers also use old ancient systems of feeding and watering systems that allow a lot of feed and water wastage. Litter damping can also cause disease problems and increase the bedding cost. The common brooding systems encountered in Malta are the gas radiant heaters and the kerosene/diesel operated blowers. At the moment the price of 1000 calories for gas is 1.7 cents while for diesel is 6.5 cents.

Feed mills import all the raw materials to produce the feeds meaning it is more difficult to formulate a diet with many feeding ingredients. The main feed ingredients used in the poultry feed are soya bean meal (44%) and maize. In the case of layers, there are two feeds for pullets and one feed for layers. There are four main feed mills in Malta and one in Gozo. The feeding programme consists of only two feeds, the starter and the finisher. The starter is fed for the first 3 to 4 weeks and the finisher is fed for the last 2 to 3 weeks. The starter is found in a crumbled form while the finisher is found as pellets.

Birds are slaughtered between the fifth and the sixth week at an average weight of around 2 to 2.4 kg live weight. The slaughterhouse supplies the farmer with the crates. If the farm size is large (say more than 3,000 broilers per batch) the batch will have to be slaughtered on more than one day due to insufficient slaughterhouse capacity does not slaughter more than this amount per day. At present there are five active slaughterhouses, one in Gozo and four in Malta. These plants have invested significantly to come into line with the EU Regulations and others are still restructuring and may open in the future. The active slaughterhouses are slaughtering between 3,000 to 5,000 broilers per day, 5 times a week, with a slaughter capacity at least 5 times higher and suggesting a probable consolidation of the sector in the future

There is one cutting plant on the island that buys poultry carcasses from slaughterhouses and cuts them into different cuts, packs and sells them to retailers and distributors. This plant has also invested significantly to come into line with the EU Regulations. Some slaughterhouses are also intending to introduce the door-to-door selling or open their own butcher shops.

Possibilities do exist to create a vertically integrated value chain based on contractual relations between stakeholders. Major weaknesses in the system include many profit centres and conflicts of interests, a number of the links in the chain and a lack of market orientation i.e. efforts along the production cycle are not focused on the final product. The creation of an improved an integrated value chain could be linked to an umbrella organisation such as a poultry industry forum with the involvement of government, as national representative of sub-sector stakeholders, providing market research, day-to-day supervision, veterinary health services, regulation of production, research and development and compliance with health and veterinary standards. Development of such a chain would come through contracting arrangements between supermarkets, slaughterhouses and producers[13].

A number of appropriate actions are also needed to promote the market for fresh produce. These include the design of an advertising and promotion strategy to develop the demand for new products, improved labelling, promoting the taste aspects of fresh Maltese production or consumer value such as Omega 3 fatty acid (which reduces cholesterol) and developing a Maltese logo. One possibility is to engage supermarkets in conducting market research and identifying consumer needs as a lead activity within the value chain and communicated to other stakeholders at regular meetings. More focus also needs to be placed on research and development of final products and to introduce innovative ways of selling, for example providing restaurants with recipes to create specialised cuisine.

Specific niche products can also be identified and where premium prices can be obtained, such as the promotion of free-range broilers and layers, organic layers, super fresh or omega 3 eggs. These niche products are likely to cover 3-5% of the broiler market, and over 7% of the layer market. Currently there is a 10% price differential between fresh and frozen broilers that could be increased through better pricing strategies and reduction in costs and greater efficiency.

The range of products for further processing which draw on local tastes and ingredients could also be expanded. For example, to consider the production of sausages, chicken nuggets, chicken curry, chicken burgers, chicken with oranges and lemons or cordon bleu (mixture of cheese, chicken breast, and ham). These are currently being produced and have proved to be profitable and competitive with imported produce.

Compared to broilers, egg producers have not felt the same severity of import competition in recent years. Although there are some egg imports from Europe (mainly for the catering industry) the Maltese consumer will always prefer fresh local eggs, even if they lack in grading or uniformity. 100 million table eggs per year are produced and these numbers fluctuate little between years. The total number of layers is estimated to be around 420,000 with an output per hen housed of around 240 eggs per year and a per capita consumption of eggs in Malta of around 230.

However while egg producers presently feel under less competitive pressure issues are likely to be raised in future years. Growers will eventually have to come in line with the EU regulations especially on welfare, egg marketing and waste management. By 2007 all farmers must be in line with the waste management regulations and the nitrate directive.

In recent years the stocking density in cages has decreased by 20% according to EU regulation 99/74 and is expected to decrease more in the coming years. At the moment, the cage stocking density is 550 cm^2 per bird and by 2012 this has to increase up to 750 cm^2 per bird. This situation will require significant restructuring investments. At present most growers store manure in open fields and nutrients are flushed away by heavy rain, A few maintain covered manure clamps and follow the Code of Good Agricultural Practise (COGAP gradually being introduced by the Ministry for Rural Affairs and the Environment.

Layers of different ages are kept under the same shed making monitoring of each flock impossible and not allowing different feeding and lighting programmes to be performed. Under correct management, a layer flock usually produce around 300 eggs per hen housed per year[14] and it is recommended to keep flocks of the same age under one roof to allow improved management of lighting and feeding.

The primary commercial poultry lines used in Malta are ISA Brown and Babcock B380 and reared on the island as a parent stock. The remainder is imported as hatching eggs or pullets (16 weeks of age) from Europe. It would be useful to have other commercial lines (both white and brown layers) brought to Malta for comparison.

The marketing of table eggs is directly from the producer to the market and the main grower focus is on having a steady egg supply. Until July 1st 2005 no eggs were graded or stamped but now a welfare number and a "use by" date will be stamped on the package to have egg tractability back through the production line. Currently there is little branding or labelling and white and brown eggs are mixed in the same pack. However brown eggs are growing in consumer popularity. This is unfortunate for growers as have higher production costs, due to the higher feed consumption and the lower number of eggs produced per hen housed.

There is a need to further train growers how to promote products differently and how to differentiate production and more specifically to have a better understanding of market-oriented production. Producers need to have the skills to target the appropriate market. Producers have tried for a number of years to organise their activities into a framework of cooperation but with little success. Two registered and two informal groups exist in Malta but none of these carry out direct commercial activity.

The Koperattiva tal-Produtturi tal-Ħalib was the first poultry co-operative established in 2000, primarily for broiler production and with the aim of collectively balancing production with demand and verticalisation from the hatchery to the consumer. The co-operative began by renting slaughtering facilities, buying pullets and then slaughtering and selling broilers. Sales turnover for the group reached 2000 tons of production during 2003 (2000 chickens per day slaughtered and cleaned) and from 200 members (only 89 producing). However in February 2004 the plant was not issued with a EU approved veterinary certificate and has not operated since[15]. A number of legal issues remain outstanding, management and staff have left the group and the re-design and upgrading of the co-operative slaughterhouse will be necessary to enable it to operate again and with costs estimated to be in the region of 200,000 Euro.

The co-operative have prepared a plan for upgrading the slaughterhouse including cutting and freezing, and for integrating the poultry sector under farmer co-operative ownership and have requested financial support from the Government through SMPPMA. However as uncertainty and costs have grown more than half of growers have broken away from the co-operative and have joined a second broiler group. This second group was formed in 2002 with 54 growers and has tried to develop alongside existing slaughterhouses and meat processors, improve the marketing activities of members, improve links with Italy for chick supply and sales and to develop a recognisable quality brand, particularly for the fresh market. Even so members of this group have also suffered in recent years from competitive market pressures and delayed payments from processors and other buyers.

Potentially the two co-operatives could again create together a single producer organisation with the aims of negotiating better payment conditions vis-à-vis processors, improving chick and feed prices or producing their own quality chicks, reactivating the current slaughterhouse or leasing processing facilities from an existing plant. Discussions on these issues are currently under development and will depend on finalising a clear and supportable business plan and ensuring competent management.

Two unregistered egg production groups (representing 2/3rds of egg production) also meet informally (one on Gozo and one in Malta). Their main concerns focus on the quality of locally produced feeds, the costs of imported feeds, chicks and kerosene, waste management and welfare regulations, egg traceability and testing. Eggs are not packed and they are sold by individual producers according to three sizes but with little price differential for colour or other specifications.

During February 2005 FAO organised strategy meetings with farmer directors of all the 4 groups and there is a general consensus that a number of opportunities exist for:

- Promoting the fresh and health aspects of Maltese production, such as low cholesterol
- Developing niche national and export markets such as for Omega 3 colour yolk, small, free range or barn eggs
- Developing a Maltese poultry logo
- Selling by-products
- Better accessing EU funds available for producers organisations
- Improving the availability of reliable market information
- Improving the overall standards of farms, slaughterhouses and processing facilities
- Working more closely with co-operatives in other meat sectors
- Further lobbying Government for enforcement of the law on traceability of imported production

FAO consultants also felt that a number of other issues need to be tackled and in particular:

- The creation of a poultry forum comprising of farmers, processors, retailers, consumers and Government representatives to further develop the issues outlined above, to carry out research, to help in standardising and improving the quality of production, encourage vertical integration and to support training, advisory and veterinary support services

- Reviewing Government monitoring, regulation and enforcement activities and particularly in relation to:
  - Public health issues through (illegally) thawing imported frozen poultry
  - Incorrect labelling and packaging
  - Grower permits that will enable broiler growers to have more than 5 cycles per year
  - Stocking densities in broiler houses that reflect kg of live weight per sq m rather than ventilation capabilities
  - Enabling construction of appropriate buildings through closer consultation between MEPA and the animal husbandry section of the Ministry for Rural Affairs and the Environment as all new and upgraded constructions require planning permission from MEPA
- Encouraging a further vertically integrated value chain based on improved contractual relations between stakeholders

The authors wish to thank the APS Bank, the Livestock Husbandry Department of the Ministry for Rural Affairs and the Environment, the Co-operative APEX organisation, the Co-operative Board and individual agricultural co-operatives from across Malta and Gozo for their help and assistance during the compilation of this paper.

Notes

1 Annual sales turnover figures for 2004 1 LM = □2.5
2 5% is paid into the co-operative fund
(a) AGM held, accounts not submitted
3 Primarily in the dairy, poultry, pork, cheeselet, honey, potato and rabbit meat sectors.
4 8 in Malta and 2 in Gozo
5 Agriculture and rural development funds
6 Of higher relevance for Gozo groups
7 There is no national farmers union or similar representative body for farmers in Malta
8 The APEX has nine elected board members, four of which are from agricultural co-operatives
9 The European representative body for farmers and their co-operatives and based in Brussels
10 A more detailed report and series of recommendations have been prepared, however this section provides a summary of some of the key issues, conclusions and recommendations
11 From both EU and non EU countries
12 Vaccinated against Newcastle disease
13 In the United States approximately 99% of all broilers are produced under contract
14 Compared to the current average of 240 in Malta
15 Before accession there were sixteen poultry slaughterhouses operating in Malta and today only five are operating and certified to EU standards

KYRIACOS PATSALOS

PRODUCER ORGANISATIONS IN THE EU-THE SITUATION IN CYPRUS

Introduction

This paper presents an overview of Producer Organisations (POs) in the European Union (EU). It concentrates first on the role and organisational set up of POs in the fruit and vegetables sector, since this sector represents an important component of agricultural output. In turn, the paper summarises the current regime of POs in Cyprus, and highlights the achievement to date following the country's accession to the EU on the first of May 2004.

Article 38 of the Treaty of Rome signed on the 25^{th} March 1957 establishes the legal basis for the development and setting up of the "Common Markets" within the framework of one Common Agricultural Policy (CAP). Through article 40 of the same treaty, among others, the legal basis was laid down for the establishment of Common Markets for several Agricultural Products.

Since then Common Market Organisations (CMO) for several agricultural products have been in place in the EU. Examples of such CMOs are the following:

The CMO for fruit and vegetables, for wine, for olive oil and table olives, for arable crops, for bananas, for tobacco, for several livestock products, and others. The measures and means employed through the CMOs of the above products are different. It is noted that one of the first CMO to be established, traced back to 1962 (Council Regulation 23/62), more comprehensive and well organised has been the CMO for fruit and vegetables sector. It has to be emphasised that Producer Groups (PGs) or POs play an important role towards the effective implementation of several measures. However, not all agricultural products governed by CMO have PGs or POs.

Until 1999, through Commission Regulation 952/97, aid was provided to PGs and their Associations for several livestock products (beef, dairy products, poultry meat and eggs, pork etc), olive oil, wines and wine grapes, among others. With the enforcement of Council Regulation 1257/99 for rural development, C.R. 952/97 was repealed.

In order to achieve the same objectives through the establishment and operation of PGs by the new ten Member States from 1st of May 2004 onwards, aid has been provided for 5 years after recognition by the competent authorities. The aid covers the expenses of setting up a PG. The legal basis for the establishment, recognition and granting of aid are the Accession Treaties of the new ten Member States, the Council Regulation 1257/99 and the relevant national Laws of these new Member States. In this connection, Cyprus included in its relevant national Law important agricultural products for establishment and recognition of PGs to help improve product quality and competitiveness and protect the environment.

1. Common Market Organisation of Fruit and Vegetables in the EU

The fresh fruit and vegetable regime was reformed in 1996. The sector has been characterised by rapid fluctuations in supply and demand for products which, on the whole, are highly perishable. The objectives of the regime are to achieve balance between supply and demand at prices which are fair to producers, to encourage specialisation within the European Union, while taking account of trade with third countries, to promote environmentally-sound cultivation techniques, production methods and waste management practices. The reformed regime aims to create a more market oriented sector, by providing aid to POs through a new operating fund and reducing the role of subsidised withdrawals (intervention).

The regime applies to all fruit and vegetables grown in the EU with the exception of potatoes, wine grapes, bananas, sweetcorn, beans and peas for fodder and olives

Basic regulations

The regime is set out in Council Regulation 2200/96 that took effect from January 1, 1997. The regulation covers marketing standards; the role of PGs and POs; inter-branch organisations and agreements; intervention arrangements; arrangements for trade with third countries, including an Entry Price System, special safeguard measures for sensitive produce and export subsidies; national and community checks. An aid scheme for citrus fruit processing is laid down in Council Regulation 2202/96 and for the processing of other products (tomatoes, peaches, pears, prunes, dried figs, etc) a different aid scheme is laid down in Council Regulation 2201/96.

1.1 Producer Groups and Producer Organisations in the European Union

Producer Groups (PGs) and Producer Organisations (POs) in the fruit and vegetables sector, as well as in other agricultural sectors, are legal entities (Co-operatives registered through Co-operatives Law, and private Companies registered through the Company Law) which are formed on the initiative of producers to ensure that production is planned and adjusted to demand, to promote concentration of supply and marketing, to reduce production costs and stabilize producer prices, and to promote the use of environmentally-sound cultivation techniques, production methods and waste management practices.

Under certain conditions, relating to their composition and operating rules, PGs and POs may be recognised by Member States under the CMO. In particular PGs and POs may be recognised by the competent authority if they had at least a minimum number of producer members and covered a minimum volume of production. This minimum size of producer organisations is fixed at 5 producers by category and at EUR100.000 (article 14 of Commission Regulation 1432/2003). However, Member States may set higher minimum standards. Only recognised PGs and POs are eligible for the relevant Community assistance as it is explained later on.

In addition to POs, Member States may choose to have PGs recognised and operating for a transition period up to five years in each case and through an approved by the competent authority phased Recognition Plan. Aid is granted to the recognised PGs to encourage their formation and facilitate their administrative operation and, also, to cover part of their capital investments through special loans or directly through aid to capital investment expenditure. However PGs are not eligible for withdrawal aid as with POs.

The role of POs has been significantly strengthened in the reformed regime. In addition to having access to intervention, POs are obliged to set up a new operating fund that will enable them to carry out an operating programme.

Producers may belong either to a single "universal" PO (i.e. fruit and vegetables category) which effectively deals with all fresh produce or, alternatively, may join more specialized POs which can be set up to cover six specific categories: fruit, vegetables, products intended for processing, citrus, nuts including carobs and mushrooms. Detailed rules on recognition of POs and PGs are laid down in Commission Regulation 1432/2003.

Operational Programs and Operational Funds

Forming in advance an operational fund (OF) is obligatory in order to implement an approved project by the competent authority operational program (OP). Community financial assistance may be granted to POs which set up an OF maintained by financial contributions from its members. The Community financial aid is to be equal to the amount of member contributions up to a limit of 50% of the actual expenditure of the fund. However, the financial assistance shall be capped at 4.1% of the value of the marketed production of each PO. Such funds are to be used to finance market withdrawls or to finance OP approved by the Member States. There is a ceiling on the proportion of the fund that may be spent on financing withdrawls

The objectives of the operational programs shall be:

- To promote the use of cultivation practices, production techniques and environmentally sound management practices.
- To make financial provisions for the technical and human resources required ensuring compliance with

plant health standards and rules, and maximum permitted levels of pesticide residues. In addition they should also include several of the following objectives:

- To ensure that production is planned and adjusted to demand, particularly in terms of quality and quantity;
- To promote concentration of supply, and the placement on the markets of the products produced by its members;
- To reduce production costs and stabilise producer prices;
- To improve quality, boosting products commercial value, promotion of the products targeted at consumers, creation of organic product lines, promotion of integrated reduction or other method of production respecting the environment, and the production of withdrawls.

Detailed rules on OP and OF are laid down in Commission Regulation1433/2003. Annex I and Annex II of this regulation present the optional contents and ineligible operations/expenditure of OP, respectively.

Association of producer organisations (APO)
It is a voluntary, legally constituted group of recognised POs who wish to submit a joint operational program, or to combine for part of their programs. It can establish, submit, and implement an OP on behalf of its member POs. If it does so, the APO will be responsible for making claims and receiving aid payment on behalf of its member POs; or if the member POs wished to submit their own individual OP the APO could be charged with co-ordination, running of measures or investments which are common to two or

more POs. In this case the POs must maintain their own operating funds.

The competent authority of each Member State gives recognition to an APO after submitting a relevant application. Information should be provided in connection with the contributions of grower members to the OF of all member POs and EU grant, all paid to a separate bank account. Besides, the rules of association of this separate legal entity should be presented. Council Regulation 1432/2003, article 9, and Council Regulation 1433/2003, article 10(3), lay down detailed procedures to this effect.

It should be noted that both PGs and POs, in cases they supply fruit and vegetables (citrus, tomatoes, etc) for processing to processors approved by competent authority, are eligible for aid. Detailed rules are laid down in council Regulation 2202/96 for citrus and Council Regulation 2201/96 for tomatoes, peaches, pears, dried figs, apart from other products.

Future Perspectives

Discussions are underway in the EU for a new reform of CMO of fruit and vegetables sector. This reform will most probably be enforced in 2007, ten years after the previous one, which took place in 1997.

With regard to PG/POs possible proposals/measures will be:

- Enlargement
- Simplification
- Legal Security
- Concentration of supply and enlargement and
- New measures on crisis management

As far as simplification is concerned possible measures would be the recognition of specialised POs, to leave up to Member State to fix specific criteria of recognition and removing the limit of ten years for any measure of the OP.

Under the heading of concentration of supply and enlargement fall the following measures:

- Promotion of activities involving different POs; more incentives to be provided for POs mergers, APOs and transactional POs.
- Incentives to be provided for POs in Member States characterised by F&V production marginal (in terms of total agriculture GDP) and low-density forming systems.
- Allow top-ups with state aids for MS/regions with low level organisation and
- Allow specific transactional ad hoc support for new POs in the new Member States

2. The Present Situation in Cyprus

The Republic of Cyprus joined the European Union on the 1st May 2004. It was agreed during the accession negotiations between Cyprus and the EU that important agricultural products, including livestock products, could be eligible for aid for their setting up for a maximum period of 5 years after their recognition by the competent authority of Cyprus. However, in order to accomplish this agreement, competency, procedures, rules of association governing Producer Groups (PGs), as it was the case with PGs/POs under the CMO of the other products, should have been prepared and enforced. Consequently, by 1st of May 2004 the relevant national Laws for the recognition of PGs and POs of all eligible agricultural products were ready and enforced. Accordingly, financial aid to eligible PGs could be provided through the Cyprus Rural Development Program 2004-2006 (Measure 1.3: Granting of aid to PGs and their associations towards their costs of setting up and running at a flat rate).

Legal basis

The legal basis for the recognition of PGs/POs and their associations for these products, as well as for other products that are governed by CMO, is the umbrella national Law 164(I)/2002 and its amending Law 160(I)/2004. Detailed rules for the implementation of these Laws are laid down in national implementing Regulations No 520/2004. Annex I of these Regulations II covers products or group of products governed by CMO. Annex II of the same Regulations submits a list of products, which are not governed by CMO, but which require further support and marketing organisation. Annex I and Annex II of this paper reproduces the lists of products.

Also, in the above mentioned Law the competent authority for the recognition of PGs/POs, their associations and interbranch organisations are determined, as well as the procedures which are followed, the documentation and checks that are required and the penalties which are applied. For products of Annex I, wherever is required by Community Regulations national rules and/or procedures have been incorporated for meeting the requirements of harmonization of Cyprus Law to EU acquis.

Part IV of the implementing Regulations expresses the national minimum criteria for recognition of PGs/POs, their associations and the interbranch organisations. In a defined region a minimum number of producers and a minimum value or volume of production in the previous calendar years are determined for each product or group of products of Annex II. In addition, rules of association of PGs are laid down and their objectives are set out. The four objectives of PGs are not governed by CMO are the following:

a) Production programming is carried out according to market demand.
b) Concentration of production, preparation for trading and trading should be implemented.
c) Implementation of common rules of production (such as organic forming and ICM) should be promoted; and
d) Application of common rules for provision of information to PGs concerning production, its availability, etc must be obligatory.

PGs are legal entities, registered through Company or Co-operatives Law, on producers' decision. The statutes and the rules of association include the following most important ones:

- Producers/members of a PG should sell their whole production through their PG;
- Exceptionally up to 15% of their production could be sold by them under certain conditions set by PG;
- Each member has the right of one vote;
- Provisions for applying penalties to the members in case they break the rules must be included;
- Provisions must also be included for application of rules for accepting new members to the PG;
- Adopting a membership period of at least 3 years and written notification to the PG for intension to leave to be sent 1 year in advance
- PGs must provide to the competent authority sufficient evidence and proof that they can carry out activities that safeguard commercial, accounting and budgetary management.

The terms "main activity", "other activities" and "different activities" are defined too. Accounts concerning only the main activities will be taken into account for recognition purposes.

Finally in Part V of these Regulations, under the heading "General Provisions", rules for checks and penalties are, also, laid down. It should be emphasised that a special committee whose members are appointed by the competent authority carry out checks regularly.

After eighteen months of Cyprus' accession to the EU, twenty-two PGs/POs of products both from Annex I and II have been recognised. They are distributed as follows:

- 8 PGs in the fruit and vegetables sector;
- 6 POs, also, in the fruit and vegetables sector;
- 1 PO for bananas;
- 1 PG for tobacco;
- 1 PO for olive oil and table olives;
- 4 PGs for potatoes and
- 1 PG for beef and cattle milk.

The competent authority in Cyprus for the first level checks is the Department of Agriculture of M.A.N.R.E. and for the second level checks is the Cyprus Paying Agency, which is also responsible for granting the aids to eligible PGs/POs.

It is the policy of the Government of the Republic of Cyprus to implement simultaneously both the Acquis and national Laws, and effectively apply financial aid to POs/PGs and their associations. Financial and technical support aim to enhance the quality of produce, ensure the ability to trace produce and verify its certification, promote animal health and welfare, encourage the protection of the environment. Therefore it eventually leads to the competitiveness of the respective units.

ANNEX I

List of agricultural products governed by CMO

I. Fruit and Vegetables
II. Fruit
III. Vegetables
IV. Products intended for processing
V. Citrus
VI. Nuts (including carobs)
VII. Mushrooms
VIII. Bananas
IX. Olive oil and table olives
X. Tobacco
XI. Products of the vineyard and wine market (wine grapes)

ANNEX II

List of agricultural products not governed by CMO

I. Beef and cattle milk
II. Cattle milk
III. Beef
IV. Sheep and goat meat and sheep and goat milk
V. Sheep and goat milk
VI. Sheep and goat meat
VII. Poultry meat
VIII. Poultry eggs
IX. Pork
X. Cereals and dry fodder crops
XI. Pulses, beans and ground nuts
XII. Live ornamental plants, flower bulbs and cut flowers
XIII. Herbs
XIV. Ware potatoes and seed potatoes
XV. Bee honey and its products
XVI. Other agricultural products

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