

PETT, FRANKLIN & CO. LLP

HELPING *SHARE* GROWTH



TAX, INCENTIVES AND  
EMPLOYEE SHARE PLANS

# Mondragon 2013

## a personal perspective

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# Mondragon

- Town in Gipuzkoa region of Basque country
- An hour's drive from Bilbao
- Mountainous area of narrow valleys
- Unlikely location for an industrial centre
- 1940s impoverished neglected area
- Losing side of Civil War
- But Basque country has a long history of enterprise eg leading pre Industrial Revolution producer of iron products supplying both sides at time of Spanish Armada

# Basque Country

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# Visionary

- Catholic priest-Father Arizmendiarieta
- 1943 founds engineering college
- 1956 founds first co-op in Mondragon-Ulgor now called Fagor manufacturing refrigerators
- Now a group of 120 coops with 83,000 worker members plus tens of thousands of other non member employees
- College become Mondragon University
- Skills developed attracted other businesses so region became a major industrial area for Spain

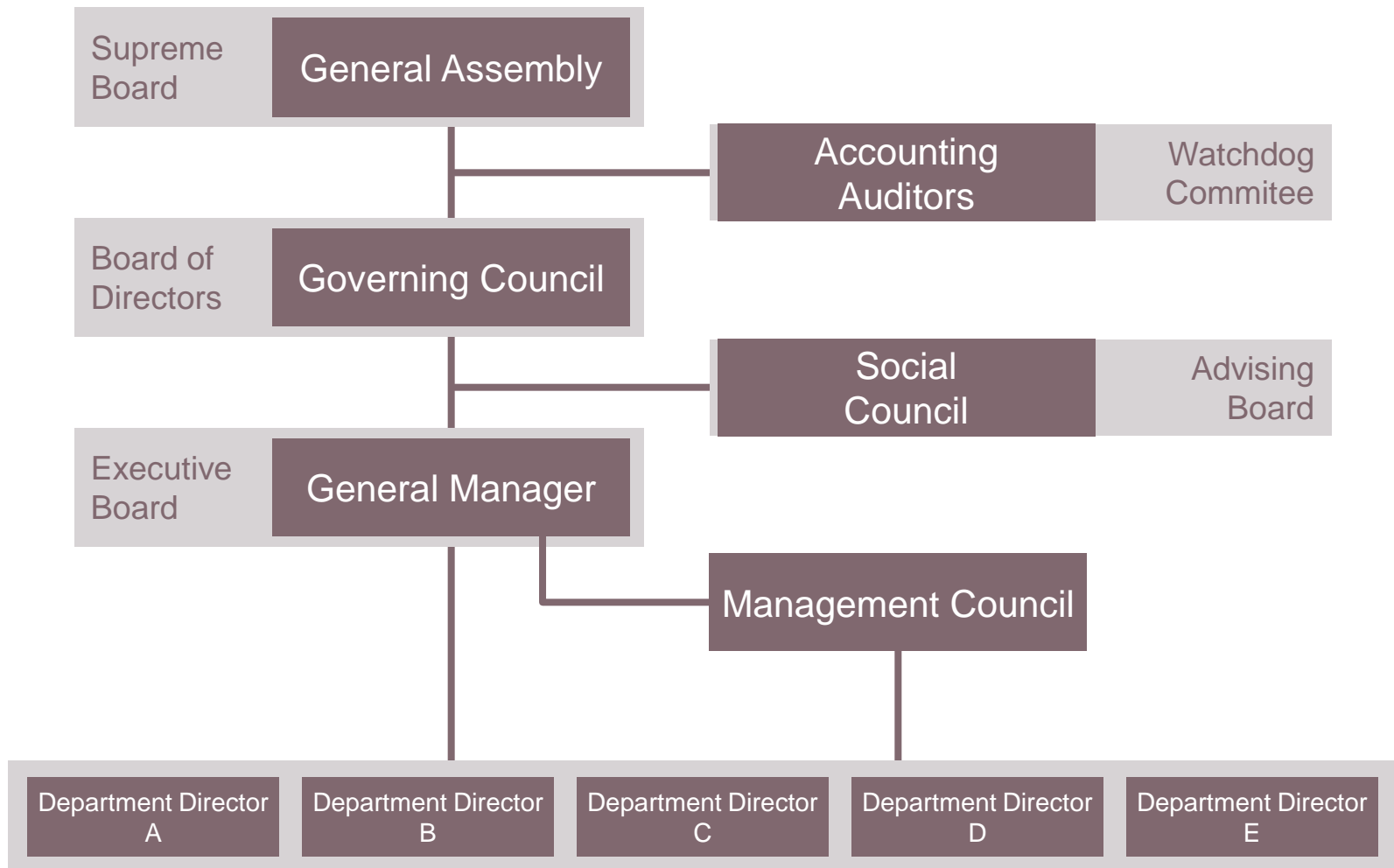
# Mondragon group

- Network of 120 independent co-ops that follow Mondragon model and work together under the umbrella of the Mondragon Cooperative Corporation (“MCC”)
- All the co-ops are based in the Basque country but many have operations in the rest of Spain and the rest of the world
- 7th largest business group in Spain

## Coop power structure

- Conventional operational management structure
- Answerable to worker members not shareholders (also report to coordinating MMC HQ)
- Key decisions made by members at annual General Assemblies: Democratic 1 member 1 vote not capital invested
- Elects a board which appoints managers
- Elects other committees to promote social objectives and monitor and audit management and business

# Basic Structure within a Cooperative



## Members

- Normally workers in the coop, but can include retired workers and collaborators( members of other coops who have contributed to this coop eg at research centres
- Bank and retail coops also have consumer members who can elect representatives to General Assemblies



# Worker Member

1. Initial Capital Contribution € 15,000 (5 years)
2. 1 member 1 vote
3. Annual profit share
4. Accumulated –paid out on retirement/leaving (c/f with John Lewis and annual pay outs)
5. Annual dividends on accumulated capital
6. Worker member invested capital important source of capital for co-ops
7. Opportunity for worker members to accumulate over working lifetime significant but not massive personal wealth
8. Akin to partnership model with moderate (salary and dividends) rather than maximum drawings
9. Pre recession average member on retirement-€ 130,000

# Status of worker members

- Essentially self employed (sort of partnership)
- Do not qualify for many Spanish social welfare benefits eg sick pay ,redundancy pay and health insurance (but do get state pension)
- Employees and co-ops pay reduced social security contributions but have to fund sick pay ,health insurance etc privately
- Non unionised

# Egalitarian Remuneration

- Minimum salary €15,000
- Original pay range 1 to 3 lowest to highest
- Much wider now to reflect market pressure, specialist skills and different businesses
- 1 to 7 ,1 to 11
- Senior management still part of local community

# Membership Rules to enter in MONDRAGON

- ✓ Relocation of staff among cooperatives.
- ✓ Restructuring results (from the gross profits).
  - . Within the sectorial groups (>15%-<40%)
  - . Within corporative funds in MONDRAGON (Investment Fund 10%) (Education Fund 2%) (Solidarity Fund 2% - for compensation in case of losses).
- ✓ Solidarity in profit distribution (net profit of each co-op)
  - . 10% Fund of Education (Law 10%)
  - . 45% Fund of Reserve of Co-op (Law 20%)
  - . 45% Returns to workers → Capitalize → Interest <7,5% in cash
- ✓ Initial capital (15.000 euros in 2012).
- ✓ Solidarity in compensation .
- ✓ Reporting of data to MONDRAGON Headquarters.
- ✓ Not internal competition between co-ops within MONDRAGON

## Structure of the power

	POWER	Factor of production (Tool, Resource)
Conventional Companies (Sociedades Anónimas)	Capital	Labour
Cooperatives	Labour	Capital

# Government support

- Founded in Franco's Spain – hostile/indifferent
- Democratic Spanish government now supportive of co-ops
- Autonomous Basque government very supportive (eg Reduced CT rate of tax ,planning approvals, R&D funding)
- Co-ops very important to Basque economy 120 Mondragon co-ops but not alone 700 co-op businesses overall for a population of only 2million.

## COOPERATIVES WITHIN MONDRAGON

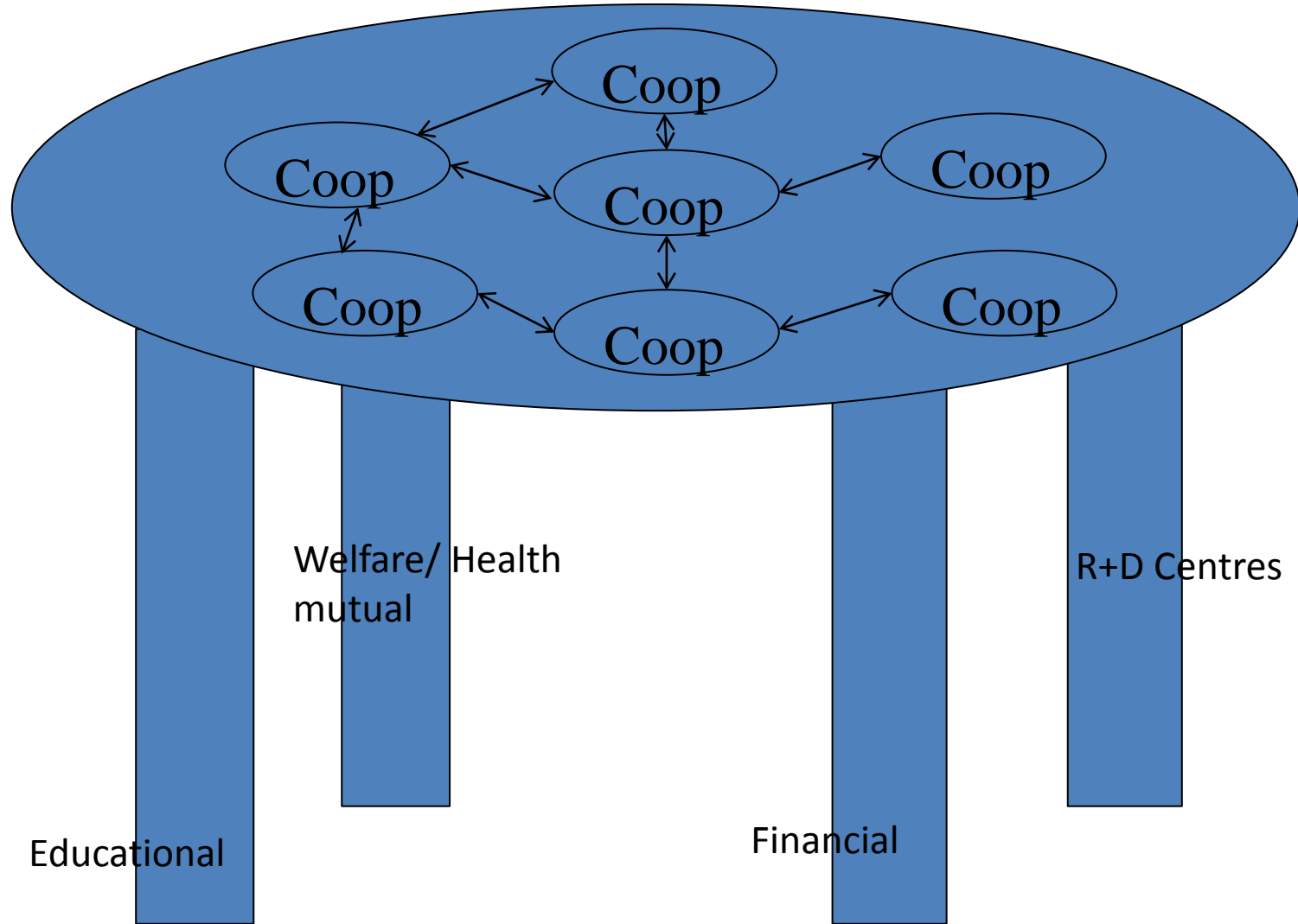
■ Industrial	<u>87</u>
■ Finance (Caja Laboral)	<u>1</u>
■ Consumer (Eroski)	<u>1</u>
■ Agricultural	<u>4</u>
■ Education	<u>8</u>
■ Research and Development	14
■ Services (Consulting, Engineering, Food, Insurance, ...)	5
■ Total cooperatives	120

# Our Organisation





# Intercooperation



# MISSION

Mondragón Co-operative Corporation (MCC) is an entrepreneurial entity with deep cultural roots in the Basque Country, created by and for the people, inspired by the Basic Principles of their Co-operative Experience. It is committed to the community, to the improvement of competitiveness and to the satisfaction of customers, to ***create wealth within society through entrepreneurial development and job creation, preferably membership-jobs in co-operatives.***

# Bank

- Caja Laboral
- Founded in 1959
- 20 years ago banking functions were split from venture capital & MCC HQ functions
- 2<sup>nd</sup> largest bank in Northern Spain
- Co-ops free to use other banks

# MCC HQ

- Modern corporate HQ in Mondragon
- About 60 employees
- Feels like an HQ of a large corporation
- Each co-op sends HQ monthly financial reports
- HQ oversees new developments, research and expansions support to loss making coops
- Co-ordinates large scale investment funding eg funding from external banks
- Manages peer to peer lending surplus staff relocation, closure of failing coops ,opening of new co-ops
- Custodian and promotion of cooperative values
- Encourage inter co-op cooperation

## Innovation

- 14 co-ops are research centres employing 2000 scientists and engineers. Funded by conducting research for other co-ops, centrally by MCC HQ and some funding from government and EU
- EG Newly formed co-op specialises in high tech equipment for foundry industry 50 jobs created so far each with average capital investment of Euros 500,000 per job.

# INNOVATION IN MONDRAGON

**716** patents

**165** M euro invested in R+D+I in 2011

**14** Research and Development  
Centers

**1.885** people in Research Centers

In 2011 Participating in **76** R+D  
projects (39 of them internationals)



# Mondragon University

- Focused on a large engineering science and technology faculty
- Other main faculty is a modern business school
- Traditionally 60%+ of engineering graduates go on to work in a co-op
- Also teacher training and Basque cooking

# CHALLENGES IN NEW SECTORS

- 1- New energies
- 2- Health+Food (Biotech, Biomedic)
- 3- New Inf+Com Technologies
- 4- The third age (elderly people sector)
- 5- New materials (electric car, aeronautic, railway)





# Lagun Aro

- Mondragon private insurance co-op
- Provides members with social benefits
- Health insurance
- Sick pay
- Redundancy pay
- Top up to state pension

# Response to Globalisation

- Source components from outside MCC if right quality and cheaper
- Many foreign operations set up over last 20 years
- Try to retain in Spain high value production, customer service , and design jobs
- Major emphasis on research and development
- Cooperative principles eg peer to peer lending and sharing knowledge

# MONDRAGON WORLDWIDE



## Lessons of foreign expansion

- 34 co-ops set up foreign operations. In addition to jobs created abroad, jobs at home also increased by 25%
- Co-ops that did not expand abroad experienced an 11% fall in jobs at home over equivalent time period

# Evolution

- Wider pay ranges permitted
- Large co-ops (500+) allowed
- 20 % non member workers limit exceeded
- Non-member subsidiaries permitted
- Major global expansion

## Red lines

- Minimum but meaningful capital investment for membership
- Bonuses accumulated over working lifetime
- Innovation and research stressed
- No external equity investment in co-ops
- Pay ranges limited
- Legal and social barriers to external trade sales of co-ops
- General Assemblies final say with 1 member 1 vote regardless of individuals seniority or capital invested

# Trade sales of co-ops ?

- Possible , members would realise gains
- But has never happened
- 2/3 rd majority of members required
- Risk of losing jobs if ceased to be a co-op
- Would be breach of co-operative values ,not socially acceptable, coops created to be durable not for exit events and not just for benefit of current members, and a sale would be seen to be at expense of future members
- Mondragon co-ops are not about Getting Rich Quick
- Failed attempt to buy bank
- But what would happen if membership was significantly extended to employees outside the Basque country where social pressures to maintain co-operative values were weaker?

# Hard Times - today

- Fire non worker -member employees
- Worker – members vote for pay cuts and negative bonuses ( return of members accumulated capital)
- No dividends on members capital
- MCC co-ordinates short term peer to peer lending between coops
- MCC co-ordinates temporary secondments of surplus members to other profitable co-ops
- For failing co-ops MCC manages closure programme and seeks to find new jobs for members elsewhere in group



# Unemployment

- Over 27 % in Spain as a whole
- Over 50% of young people unemployed
- Towns with Mondragon co-ops have the lowest rates of unemployment in Spain and pre recession usually had low or nil unemployment

## Problems 1

- Difficult to sack an underperforming worker member ( preference for arbitration)
- Prolonged Spanish and European recessions is putting model under strain eg pay cuts, negative bonuses, contraction of some older co-ops and movement of activities abroad, some co-ops potentially overmanned and uncompetitive and threatened with losing markets and ultimately closure

## Problems 2

- Growing numbers of employees who are not worker members in Spain and rest of World?
- How do they extend co-operative ownership to workers in foreign subsidiaries and still preserve cooperative values?
- A few disillusioned co-ops have started leaving MCC umbrella

# Basques a special people

- Small population 2-3 million fiercely independent, resisted colonisation
- Long history of enterprise, self help and technical skills
- Unique language and geographical isolation surrounded by mountains and sea fostered a special identity
- No Basque kings and limited aristocracy
- Conducive for a business vision built on co-operation, trust, enterprise, sharing and self management in contrast to Anglo Saxon vision which emphasises individualism and the importance of the leader

## Reproducible?

- Some say key to success of Mondragon is uniqueness of the Basques
- Others say the circumstances there allowed a business model to flourish which elsewhere has rarely been tried or has been misunderstood and denied the opportunity to develop.
- Foreign subsidiaries?
- African Mondragons?

# The **keys** corporate values

## **CO-OPERATION**

Owners and protagonists

## **PARTICIPATION**

Commitment to management

## **SOCIAL RESPONSIBILITY**

Distribution of wealth based on solidarity,  
and involvement in the community

## **INNOVATION**

Constant renewal



# Contact details

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