



**CO-OPERATIVES UK**

January 2014

## **Submission to the Kelly Review: Co-operative Governance**

### **1 About Co-operatives UK**

- 1.1 Co-operatives UK is the national trade body that campaigns for co-operation and works to promote, develop and unite co-operative enterprises. We have a unique role as a trade association for co-operatives. We work to promote co-operative businesses across all sectors of the economy – from retail and finance where co-operatives are most recognised to key growth areas such as renewable energy, agriculture and education.
- 1.2 Together the co-operative economy is worth some £35.6 billion, is owned by nearly 13 million adult members in the UK and has grown by nearly 20 per cent since the start of the credit crunch.
- 1.3 Co-operatives UK has 75 per cent of the UK co-operative sector in direct or indirect membership.

#### **Key Points**

- The relevance for the wider co-operative business model of any lessons learned from the Kelly Review should be considered within the context of a diverse co-operative movement in the UK and worldwide.
- If lessons learned from the Kelly Review result in hypotheses or recommendations that are considered of relevance to the wider cooperative sector, then it may be helpful to explore these with Co-operatives UK at an appropriate point, as a representative and expert body on the sector.
- We have indicated to our members that we will review our own governance codes in the light of any recommendations on co-operative governance in consumer societies that emerge from the Kelly Review.

## 2 Context

- 2.1 We welcome the involvement of Sir Christopher Kelly in helping the Co-operative Group, and by extension, the wider co-operative sector to learn from the events surrounding the Co-operative Bank. Prior to the establishment of this review, Co-operatives UK's Secretary General, Ed Mayo, called for a process of deep learning and published online a set of open questions.<sup>1</sup>
- 2.2 The published terms of reference for Sir Christopher Kelly's review include an intention to: "...identify lessons which can be learnt to strengthen *The Co-operative Bank and the wider Co-operative Group, and the co-operative business model generally.*" From this we anticipate that the outcome of the Kelly Review will be of interest to the co-operative movement as a whole, and as association for co-operatives and mutuals in the UK, we are eager to inform the relevant areas of work, so that lessons properly reflect the co-operative business model generally, of which the Co-operative Group is not necessarily a typical example.
- 2.3 We also note an intention to: "...investigate the robustness and timeliness of the Board's... strategic decisions." An investigation of strategic decisions in any business may of course include a focus on the quality of governance, including consideration of the handling of risk, and the competency of decision-making and subsequent implementation.
- 2.4 Our submission to the Review therefore addresses these two keys topics where we are well placed to contribute:
- Perspective from the co-operative sector in the UK and the movement worldwide.
  - The governance of UK co-operatives, including the role of Co-operatives UK.

## 3 The UK co-operative sector

- 3.1 We ask that lessons learnt by Sir Christopher Kelly that may be relevant to "*the co-operative business model generally*" are placed within the context of a diverse and growing UK and international co-operative sector.
- 3.2 What is a co-operative? Co-operative enterprises are member owned business with some distinctive characteristics in terms of form and ethos.
- 3.3 At an abstract level, the nature of co-operatives is defined by a co-operative identity statement proclaimed by the International Co-operative Alliance (ICA) in 1995. These were endorsed by United Nations Guidelines in 2001 and by an International Labour Office Recommendation (193) in 2002, and have been written into many co-operative laws around the world.

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<sup>1</sup> <http://edmayo.wordpress.com/2013/07/12/an-open-set-of-questions/>

- 3.4 In practice, there is a diversity of co-operative forms, in the UK and overseas. You can form a co-operative in the UK using a variety of legal forms. There is continuous experimentation around key issues, such as the nature of membership, interest in community benefit and new models of financing.
- 3.5 Apart from the investors of capital, there are three main economic stakeholders in any business: its consumers, the producers who supply inputs to or take the outputs from the business, and its employees.
- 3.6 In a co-operative, usually one of these other stakeholders is put at the center of the business as member owners.
- 3.7 The advantages to stakeholders of co-operating are obvious; together they can channel the value added from the business to themselves rather than to investor-owners or to 'middlemen'. They are co-operating in order to compete:
- Consumer owned businesses provide people with consumption goods at the lowest possible price and with a guarantee of good value, and so make their income go further.
  - Producer owned businesses enable individual self-employed people and other businesses entities to come together to achieve economies of scale and improvements in their business offer.
  - Worker owned businesses provide people with an income, but also are a way of gaining control over the conditions under which they labour, providing what the International Labour Organisation calls 'decent work'.
- 3.8 A number of co-operatives businesses are hybrid – or multi-stakeholder - enterprises. These deliberately offer different categories of membership to more than one stakeholder. The Eroski retail co-operative in Spain, for example, has employee and customer members. Social co-operatives in Italy that provide care services to disabled and vulnerable people are, by law, required to offer membership to employees, service users and carers.
- 3.9 There are therefore four groups of co-operatives: consumer owned, producer owned, employee owned and multi-stakeholder combinations or hybrids of these.
- 3.10 Because co-operatives are member-owned, they are generally not subject to stock market listing. Unlike the situation for PLCs, teams of analysts are not employed to study their performance and the financial press often omits to report their results. As a consequence, there has been a tendency to marginalise the role of the sector.
- 3.11 For this reason, Co-operatives UK has developed since 2007 a systematic research database, drawing on published accounts of the most recent financial year from co-operatives. This data offers a systematic and rigorous account of the performance of co-operative enterprise.

- 3.12 There are over 6,000 individual co-operative enterprises in the UK, utilising a variety of business models, and meeting needs in a diverse range of sectors from retail and finance to agriculture and energy. In 2012 the combined annual turnover of the UK's co-operative economy was approximately £35.6 billion, and co-operatives served almost 13 million adult members.<sup>2</sup>
- 3.13 The sector contains a diverse range of co-operative ownership models:
- Consumer owned co-operatives account for 49.9% of the sector by number, and 49.5% by turnover.
  - Worker owned co-operatives account for 8.1% of the sector by number and 27.5% by turnover.
  - Enterprise owned co-operatives account for 16.1% of the sector by number and 19.3% by turnover.
  - Mixed ownership co-operatives account for 17.3% of the sector by number and 3.6% of the turnover.<sup>3</sup>
- 3.14 To further emphasise diversity, the size of co-operative businesses in the UK varies hugely, with the vast majority meeting the definition of SMEs or micro businesses. Of those co-operatives for which turnover information is available, 12.5% have an annual turnover of £1 million or more, and 65% have an annual turnover of under £250,000.<sup>4</sup>
- 3.15 The dynamic growth in the sector is demonstrated by the fact that since 2008 the combined turnover of the co-operative economy has grown by 23%, the number of co-operatives has risen by 28%, and there has been a 36% increase in the number of memberships.<sup>5</sup>

#### **4 The international co-operative movement**

- 4.1 It may be helpful to consider any lessons learnt on "*the co-operative business model generally*" in the context of a diverse international co-operative movement.
- 4.2 The world's largest co-operatives have a combined turnover of \$2,578.5 billion (USD), and serve members in every part of the world. There are 1,465 co-operatives across 42 countries that boast an annual turnover of over \$100 million (USD)<sup>6</sup>.
- 4.3 The strongest economic sectors for co-operatives worldwide are insurance, agriculture and food industries, and wholesale and retail.<sup>7</sup>

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<sup>2</sup> Co-operatives UK (2013) '[Homegrown: the Co-operative Economy 2013](#)'

<sup>3</sup> Ibid

<sup>4</sup> Ibid

<sup>5</sup> Ibid

<sup>6</sup> World Co-operative Monitor (2013) '[Exploring the Co-operative Economy: Report 2013](#)'

<sup>7</sup> Ibid

4.4 Worldwide the co-operative movement is represented through the [International Co-operative Alliance \(ICA\)](#). The ICA is the global guardian of the co-operative identity, as set out in internationally recognised '[Values and Principles](#)', and displayed through the [Co-operative Marque](#).

## **5 Co-operative governance and Co-operatives UK governance standards**

5.1 The strength of the co-operative model is held to be the fact that ownership rests with those who are most closely involved in the life of a business. These members bring knowledge, commitment and, arguably, an alignment of interests with long-term performance rather than short-term gain.

5.2 The nature of membership, of course, varies across different types of co-operative, with different ways of being involved. But, for all the diversity of practice, the two characteristics that are shared by all outstanding co-operatives are member engagement and good governance.

5.3 Without these, and in the absence of some of the accountability mechanisms around public companies with traded shares, such as financial analysts, institutional investors and the scope for take-overs, the strength of the co-operative model becomes instead its weakness.

5.4 A co-operative board has to act in accordance with the co-operative values and principles, whereas the board of an investor-owned business simply has to provide responsible leadership. There is therefore a stronger emphasis in co-operatives on active participation. Members are encouraged to play a part in governance, whereas shareholders in listed companies simply monitor governance by the board. The co-operative board is expected to engage with active members and maintain close relations, whereas the investor-owned business board is charged only to ensure dialogue with major shareholders.

5.5 Co-operatives UK operates a number of quality standards, to guide co-operatives in relation to good governance. These include the '[Corporate Governance Code for Co-operative Societies](#)', the '[Worker Co-operative Code of Governance](#)', and, a standard currently under development for agricultural co-operatives.

5.6 The Corporate Governance Code for Consumer Co-operative Societies is a self-regulation quality standard intended to ensure that co-operative businesses are well run and meet their members' needs. The code was first launched by Co-operatives UK (then the Co-operative Union) in 1996.

5.7 This code has now been comprehensively revised, after a period of open consultation in the co-operative sector. The new code applies to all the major consumer retail co-operatives from 2014.

5.8 The code sits alongside the usual legal requirements set out in law or, from time to time, by the Financial Conduct Authority. Co-operatives working in or with subsidiaries operating in regulated sectors, such as banking or energy, also have to comply with duties set out by the regulators in those sectors, reflecting the specialist expertise that is often required.

- 5.9 The co-operative code is based on the UK Corporate Governance Code, with considerable overlap, for a good reason. Good governance is in many respects about the same underlying principles – such as the accountability of a Board to the owners, the role that a Board has in directing but not managing activity, the duty a Board has in relation to due diligence, risk management and so on.
- 5.10 The major areas in which the new Corporate Governance Code for Consumer Co-operative Societies has been strengthened include:
- The handling of risk: including who is responsible, how it is managed, what the appetite for taking on risk is and what the internal controls and risk management looks like.
  - Board skills and composition: including the balance of newly elected and experienced board members, board evaluation and ensuring that directors have the appropriate skills to undertake their role.
  - Equalities: recognising the benefits of a diverse Board and removing references to any upper limit age rule.
  - Fraud: ensuring transparency in the democratic process, with particular reference to ensuring that election and voting procedures are free from fraud and undue influence.
- 5.11 The revised code sets out twenty high level principles, spanning 163 separate provisions, which societies are required to report against, on a ‘comply or explain’ basis, to their own members in the Annual Report as well as to Co-operatives UK, which monitors compliance with the code.
- 5.12 The ‘Corporate Governance Code for Consumer Co-operative Societies’ was last updated in November 2013. We are mindful that the findings of the Review may impact on our work in this area.
- 5.13 We have also developed a guide for smaller co-operatives, [‘Simply Governance’](#), and, an online Governance Audit tool.

## **6 Concluding remarks**

- 6.1 We wish the Review well and look forward to your findings.
- 6.2 We suggest that the relevance for the wider co-operative business model of any lessons learned is considered within the context of a diverse co-operative movement in the UK and worldwide. If lessons learned from the Review result in hypotheses or recommendations that are considered of relevance to the wider cooperative sector, then it may be helpful to explore these with us at an appropriate point, as a representative and expert body on the sector.
- 6.3 Co-operatives UK works to continuously monitor, improve, and promote good governance standards in the UK co-operative sector. We will therefore welcome the findings of the Kelly Review if there are particular lessons relating to co-operative governance. We have indicated to our members that we will also review our own governance codes in the light of any recommendations on co-operative governance in consumer societies that emerge from the Review.

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