



# **DEPARTMENT OF AGRICULTURAL ECONOMICS**

## **LECTURE NOTES**

### **Cooperative organization and Management (AgEc 3105)**

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WOLISO CAMPUS**

## Chapter 1: Introduction

- Definition of a Cooperative by the ICA Cooperative Identity Statement Prepared by Daman Prakash, Director\* (1995)
- “A cooperative is an autonomous association of persons united voluntarily to meet their common economic, social and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise.”
- This definition is intended as a minimal statement; it is not intended as a description of the ‘perfect’ cooperative.
- It is intentionally broad in scope, recognizing that members of the various kinds of cooperatives will be involved differently and that members must have some freedom in how they organise their affairs.
- The definition emphasizes the following characteristics of a cooperative (5)
- [A] The cooperative is autonomous – it is as independent of government and private firms as possible;
- [B] It is an association of persons. Cooperatives are free to define ‘persons’ in any legal way they choose – individual and or legal persons;
- [C] The persons are united ‘voluntarily’. Membership should not be compulsory.
- Members should be free to join or to leave;
- [D] Members of a cooperative ‘meet their common economic, social and cultural needs’. Indeed in the future helping to provide a better way of life – cultural, intellectual and spiritual – may become one of the most important ways in which the cooperatives can benefit their members and contribute to their communities;
- [E] The cooperative is a ‘jointly-owned and democratically-controlled enterprise’.
- Within the cooperative control is distributed among members on a democratic basis.
- The dual characteristics of ownership and democratic control are particularly important in differentiating cooperatives from other kinds of organisations.

### 1.1. Concept and definitions of cooperatives

- What is the purpose of a cooperative?

- To allow individuals to come together and pool their resources in order to reach common goal which would be difficult for them to achieve as individuals.
- Cooperatives are enterprises which help their members cooperate together to solve problems they share.
- The International Co-operative Alliance, a non-governmental organization which is the umbrella organization for cooperatives worldwide, defines cooperatives as
- An autonomous association of persons united voluntarily to meet their common
  - economic,
  - social and
  - cultural needs and aspirations
  - through a jointly-owned and democratically-controlled enterprise.
- Another widely accepted cooperative definition is the one adopted by the United States Department of Agriculture : A cooperative is
  - a user-owned,
  - user-controlled business
  - that distributes benefits on the basis of use.
- This definition captures what are generally considered the three primary cooperative principles: user ownership, user control, and proportional distribution of benefits.

### **1.2. Scope of cooperatives**

- A legally incorporated business, owned by its members who use its services. Like other businesses a co-op:
  - ❖ Requires start up capital/equity
  - ❖ Generates revenue to cover its costs
  - ❖ Must provide quality services
  - ❖ Can distribute profits back to its owners
  - ❖ Can retain profits for future needs
  - ❖ Goal is financial self sufficiency
  - ❖ Have limited liability for owners
  - ❖ Can borrow money/sign contracts
  - ❖ Pay business taxes

### 1.3. Objectives and Benefit of cooperatives

- The cooperative is a non-profit-making service enterprise whose objective is to
  - ❖ free its members from any exploitation they are suffering by strengthening them in their economic role as
  - ❖ purchasers,
  - ❖ workers,
  - ❖ sellers,
  - ❖ borrowers,

#### **Benefit of cooperatives.**

- Combines the wealth and resources of many individuals and harnesses (join) them in a united way.
- Structured so that individual interest does not dominate collective interests.
- Individual dominance can adversely effect the welfare of different social groups.
- Bargaining Power
- Market Access
- Community Strength
- Political Action
- Reduced Costs
- Quality products and services
- Economic Enhancement
- Competitive Yardstick

#### **Learning activity**

Can you mention any form of local organizations in your community?

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Have you ever heard of cooperatives? If yes, what do you think are they?

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## Chapter 2

### Evolution of cooperatives

At the end of this chapter you will be able to discuss:

- ❖ Cooperative development in the world
  - Developed countries
  - Developing countries
- ❖ Cooperative development in Ethiopia

#### 2.1. Cooperative development in the world

- It is difficult, even impossible, to pinpoint the exact origin of the first cooperatives.
- The cooperative movement as such appeared in Europe in the 18<sup>th</sup> century, following
  - ❖ the economic,
  - ❖ social and
  - ❖ Demographic changes caused by the Industrial Revolution.

The origins of the cooperative movement in industrialized countries

- The effects of this revolution were certainly industrial and commercial dynamism, characterized by
  - ❖ a rise in urban populations,
  - ❖ a reduction in wages and exploitation of workers, particularly women and children.
- In addition,
  - ❖ an increase in the cost of living,
  - ❖ adulteration of foodstuffs and
  - ❖ a rise in unemployment are other characteristics of this period.
- This situation led certain thinkers and humanitarians to seek
  - ❖ a solution to the growing unhappiness of the poor,
  - ❖ to dream up a new system or
  - ❖ even a new form of social organization.
- This way of thinking had a considerable impact in Great Britain and France but also in Germany.

- In Great Britain one of the main thinkers was Robert Owen (1771-1858), known by some as the father of cooperation.
- He thought it would be more economical to deal with the poor in groups rather than individually; hence his proposal for what he himself called villages of cooperation.
- He first conceived these villages as a solution to the problem of unemployment and misery.
- He wanted to help the poorest villagers to acquire communal property and to take up work - especially farm work - which would save them from misery.
- But gradually his concept grew, these villages of cooperation became the ideal type of society towards which he wanted to thrust (push) humankind.
- Dr. William King (1786-1865) gave a more practical direction to the some what utopian (perfect) ideas of Owen.
- Like Owen, he had in mind a self-sufficient community in which the workers would produce according to their needs.
- But, contrary to Owen, he favored the involvement of the members with the outside world, in keeping with the earlier philanthropic funding concept
- His idea was to encourage the establishment of shops by and for the working classes.
- Collecting regular payments from the workers would guarantee the funding of these shops.
- Rather than getting their supplies from shops unknown to them, the workers would buy them in their own shop.
- Therefore, they would buy goods at the wholesale price to then sell on more cheaply than the going rate.
- England is the cradle of consumer coops.
- Owen and King defined the rules and principles of consumer cooperatives.
- This type of cooperative supplies goods (food, educational supplies etc.) to its members
  - ❖ at a lower cost than if they had tried to get them individually and not collectively.
- In France, Charles Fourier (1772-1837) was one of the first to propose an alternative form of cooperation, i.e. a community organization he calls “phalanstery”.
- The idea was to fight poverty with growth of production;

- ❖ for example by bringing together the different members of a canton (district, area) so that they could pool their resources, especially their land, and live together in the phalanstery.
- Charles Fourier is referring here to producer cooperatives which market directly or adapt and market the products or services of their members.
- Philippe Bucher (1796-1865) himself defined the fundamental principles of producer cooperatives:
  - i) Principle of the democratic right to vote for the representatives of the cooperative;
  - ii) Principle of equal pay for equal work;
  - iii) Principle of charitable reallocation of net assets, in other words in the event of dissolution the reserve funds will be distributed either to another cooperative or to a charitable cause or to the State
  - iv) Principle of the inevitable blurring (distorting) of the distinction between the status of the member and that of the user:
    - all the workers in the cooperative must become members of it.
    - France is the cradle of worker cooperatives.
    - In Germany, Hermann Schulze- Delitzsch (1808-1883) is considered to be the pioneer (founder) of municipal (public) cooperatives.
    - He made himself the apostle of municipal credit cooperatives after working out that lack of capital was a major problem for people living in towns.
    - His cooperatives were based on self-help in its purest form; that means no outside intervention at all, not even from the State.
    - For Schulze-Delitzsch, the cooperative had a purely economic role to play in raising revenue.
    - His other principles were
      - self responsibility,
      - equal rights for each individual within the cooperative group,
      - joint responsibility for debts by the group and
      - finally democratic self-control.
    - Friedrich Wilhelm Raiffeisen (1818-1888) for his part is regarded in Germany as the pioneer of rural cooperatives.

- His model for credit cooperatives differs from that of Schulze-Delitzsch in the sense that the
  - principle of self-help was not applied in absolute terms,
  - the building up of a capital base was in no way deemed necessary and that the reserves were distributed to another association in the event of dissolution.
- Raiffeisen's principles are:
  - the advancement of the members, as much religious and moral as material,
  - a limit on the number of group members based on the size of a village and
  - the unlimited mutual responsibility of the members.
- We can at best trace the great lines which have helped it become what it is today, that is to say a worldwide movement.
- Nevertheless, we must mention the importance of the work of the twenty eight Rochdale workers in the formation and observation of the cooperative principles.
- In contrast to the other principles or expressions of principles which were the work of individuals, the Rochdale Pioneers, composed of twenty-eight workers, were the authors of the first group approach cooperative principles history.
- That is why they are regarded as the pioneers of cooperative principles, or even of the cooperative movement itself
- It all began in 1843 after fruitless pay talks. When they did not get the rise they had hoped for, the Rochdale Pioneers without knowing exactly what they were going to do, decided to set up a fighting fund to raise start-up capital for an as yet undetermined plan. After mature reflection and influenced by Owen, they opted for the cooperative solution.
- On October 24th 1844, they registered the Rochdale Equitable Pioneers Society, a cooperative retail society.
- This meant that its members could get supplies of food and other goods at the lowest cost.
- The Rochdale cooperative thus became a model not only for all consumer cooperatives but also for all cooperatives around the world.
- To this day, the Rochdale principles dominate the world cooperative movement. These principles are the following:
  - Open and voluntary membership;



- Democratic control;
- Interest on share capital limited to 6%;
- Distribution of surplus to members in proportion to their transactions;
- Cash trading;
- Education and training for members;
- Political and religious neutrality;
- Charitable distribution of assets in the event of dissolution.
  - This brief historical reminder shows that in most industrialized countries, the cooperative institution appeared spontaneously in response to problems of the day.
  - However, it must be stressed that in most of these countries, the cooperative institution only found its definitive formula when the “working class” adopted this new form of organization.

## **2.2. The introduction of cooperatives in developing countries**

- The Industrial Revolution very soon forced industrialized countries to seek out raw materials and new outlets for their products.
- It therefore played a not inconsiderable role in the colonization of the developing countries, the objective for the colonizing countries being to increase the area of their national territory by appropriating foreign lands.
- Countries thus lost their sovereignty (power) and did so, on their own territory, in favor of the home country.

Africa, Asia, and Latin America then found themselves dominated by western countries including Great Britain, Portugal, France and Belgium.

- Once the country was conquered, the settlers ensured the promotion and development of the cooperative form of organization.
- The objective was never altruistic (humane). Cooperatives were in fact used as a strategic tool to allow people to be grouped together and goods, essential for the economy of the home country (coffee, cocoa etc.), to be collected for export.
- The development of cooperatives within the colonies has followed different forms depending on the colonizing country's origin.

- In Latin America, the promotion of cooperatives is carried out according to the ideas of European promoters, notably the Frenchman Gide and the German Raiffeisen, Schulze-Delitzsch and Haas.

On the other hand, in the Asian countries of the British Empire, the English ideas form the basis of cooperative development.

- After independence in the colonized countries, the governments of the newly independent States accorded an essential role to cooperatives especially in the development of rural areas.
- Nevertheless, in most of these countries, cooperatives remained a State-owned tool with which to control the masses.

### **2.3. Cooperative development in Ethiopia**

#### **23.1. Traditional Cooperatives in Ethiopia**

- In Ethiopia there are three well known traditional cooperatives or self-help groups
- Edir: - is one of the traditional forms of cooperatives still operating almost in all parts of Ethiopia, urban and rural.
- It is similar with burial cooperatives or organization that mainly stand for performing
  - ❖ burial ceremonies,
  - ❖ to condolence, and
  - ❖ assist financially and labor.

#### **Ekub**

- Ekub is other form of traditional cooperative or traditional self-help group in Ethiopia.
- Ekub is a financial form of traditional cooperative formed voluntarily.

It is a rotating saving and credit type association whose members make regular contributions to a revolving loan fund.

#### **Debo/ Wenfal/ Lefenty/ Jigie**

- This form of traditional cooperative or mutual help group is an important form of traditional cooperatives in Ethiopia.
- This is mainly a cooperative formed at the rural area of the different parts of the country where most of the people are farmers.
- Debo is a system of farmer's cooperation during the time of farming, weeding, harvesting, trashing, and house construction etc.

- Debo/Wenfale/Lefenty does not have a system of administration like the other form of associations
- it is based on equivalent labor or material contribution (Ox) by each farmer.

### **Cooperatives Development in Ethiopian**

Some special features of Traditional Cooperatives in Relation to Modern Cooperative. Are as follows:

- ❖ Established on the felt needs of members and voluntary membership
- ❖ Democratic control and administration
- ❖ Fair and equal compensation
- ❖ Equal contribution
- ❖ Equal participation of each member.
- ❖ Serve their members
- ❖ Cultural development and other development activities
- ❖ Political neutrality
- ❖ Equal opportunity to all members
- ❖ They can be organized at working place, living area bases.
- ❖ Though there is a dearth (lack) of consistent time series data on cooperative development in Ethiopia,
- ❖ Available data indicates the number of registered cooperatives in Ethiopia has generally increased overtime.
- ❖ There are also several non-registered groups or associations that provide functions similar to the cooperative model.
- ❖ For instance, microenterprise groups and associations are steadily increasing, especially in urban areas.
- ❖ In 1974 there were approximately 149 cooperatives, including:
  - ❖ 94 multipurpose cooperatives;
  - ❖ 19 SACCOs;
  - ❖ 19 consumers' cooperatives;
  - ❖ 17 handicraft cooperatives
- ❖ The number of cooperatives significantly increased during the Derg regime (1974-1991), with approximately 10,524 primary cooperatives having 4,529,259 members recorded.

- ❖ Cooperative organization was highly political during this time and many cooperatives were dismantled following the downfall of the Derg regime in 1991. the number of cooperatives in Ethiopia declined from 10,524 during the Derg regime to 7,366 cooperatives in 1991.
- ❖ Policy support for cooperatives provided by the current government has seen the number of cooperatives start to increase again.
- ❖ Data obtained from FCA indicates that up to 2004 there were 8,009 primary cooperatives with 4.06 million members and a turnover of ETB 327.12 million (USD 32.81 million).
- ❖ In 2005, an additional 6,072 new cooperatives were established, raising the total number of cooperatives to 14,081, with a membership of 4.23 million.
- ❖ The interest of the people to join cooperatives continued to increase steadily, with 5,066 new cooperatives established in 2006.
- ❖ This made the total number of primary cooperatives rise to 19,147 and the capital base of cooperatives expand to ETB 1.475 billion (USD 147.94 million) (FCA 2007a).
- ❖ The number of primary cooperatives further increased from 19,147 in 2006 to 24,167 in 2007.
- ❖ Approximately 18 per cent of members are female.

### Learning activity

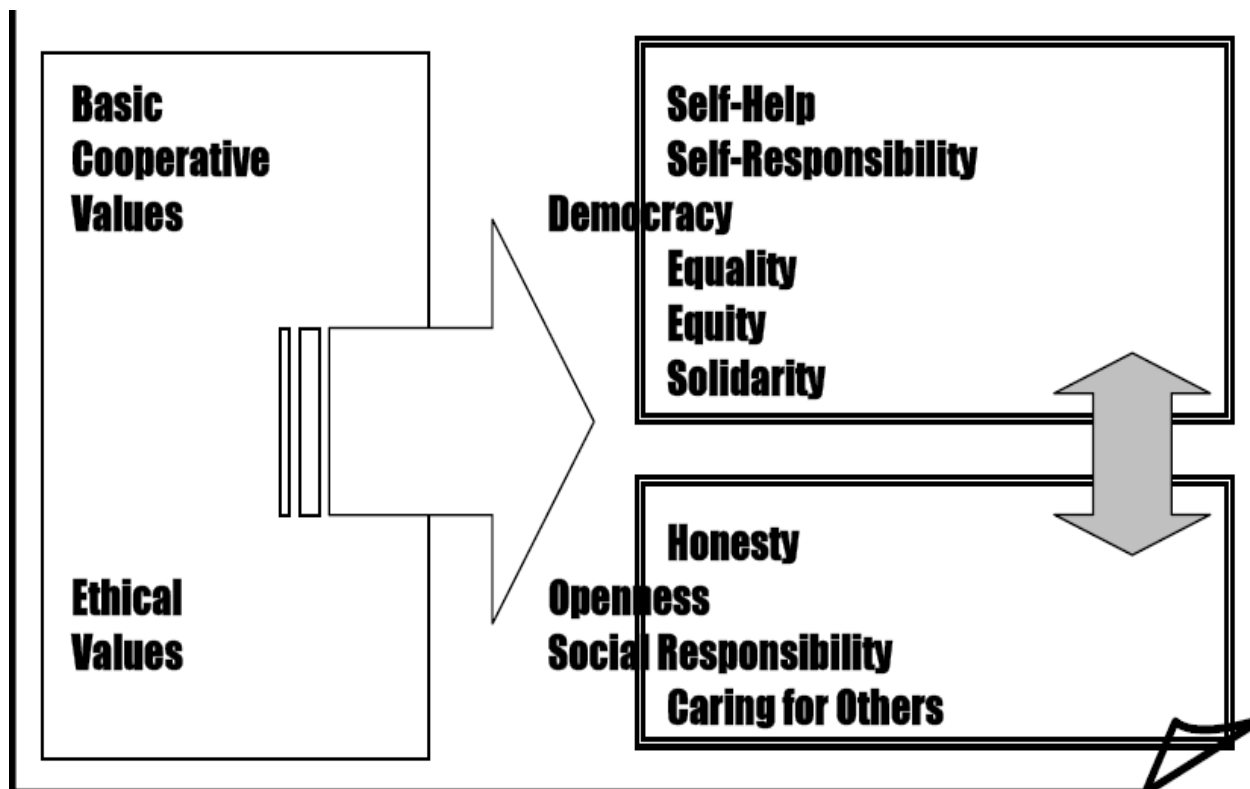
1. What are the traditional forms of organizations? Explain by giving examples  
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2. What roles do traditional forms of organizations have to the people?  
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3. Who are the important scholars that contribute to the present day cooperatives come to existence?  
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4. Discuss the difference between cooperative movement in Africa and in developed countries.  
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5. Discuss the development of cooperatives in Ethiopia.  
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6. Reflect about similar features of cooperatives at different times from your previous discussion?

## Chapter 3

### Values and principles of cooperatives

#### 3.1. The Basic Cooperative Values

- The basic cooperative values as enshrined in the definition are stated as follows:
- ‘Cooperatives are based on the values of:
  - ❖ self-help,
  - ❖ self-responsibility,
  - ❖ democracy,
  - ❖ equality,
  - ❖ equity and solidarity.
- In the tradition of their founders, cooperative members believe in the ethical values of
  - ❖ honesty,
  - ❖ openness,
  - ❖ social responsibility and caring for others.



#### 1. Self-Help

- is based on the belief that all people can and should strive to control **their own destiny**.
- Cooperators believe that full individual development **can take place only** in association with others.
- Individuals also develop through cooperative action by the skills they learn in facilitating the growth of their cooperative.
- Cooperatives are institutions that foster the continuing education and development of all those involved with them

## 2. Self- Responsibility

- members assume **responsibility for their cooperative** – for its establishment and its continuing vitality.
- Members have the responsibility **of promoting** their cooperative among their families, friends and acquaintances.
- Members also ensure that their cooperative remains **independent**

## 3. Equality

- Members, whether an individual or a group, are all equal.
  - It does not depend on the social and economic status of the member
- Equity
- Achieving ‘equity’ within a cooperative is continuing, never-ending challenge.
  - It also refers to how members are treated within a cooperative.
  - They should be treated equitably in how they are rewarded for their participation in a cooperative, normally through patronage dividends, allocation to capital reserves in their name, or reduction in charges

## 4. Solidarity

- ensures that cooperative action is not just a disguised form of limited self-interest.
- A cooperative is more than in association of members; it is also a collectivity.
- All members including the employees and the nonmembers who are closely associated with the cooperative should be treated fairly.
- This also means that the cooperative has a responsibility for the collective interest of its members.

- Solidarity is the very cause and consequence of self-help and mutual help

### **3.2. Principles of cooperatives**

- The cooperative principles are guidelines by which cooperatives can put their values into practice.
1. voluntary and open membership;
  2. democratic member control;
  3. member economic participation;
  4. autonomy and independence;
  5. education, training and information;
  6. cooperation among cooperatives;
  7. concern for community.

#### **1st Principle: Voluntary and open membership**

- Cooperatives are voluntary organizations,
- open to all persons able to use their services and
- willing to accept the responsibilities of membership, without
  - ❖ gender,
  - ❖ social,
  - ❖ racial,
  - ❖ political or
  - ❖ religious discrimination.

#### **2nd Principle: Democratic member control**

- Cooperatives are democratic organizations controlled by their members who actively participate in setting their policies and making decisions.
- Men and women serving as elected representatives are accountable to the membership.
- In primary cooperatives members have equal voting rights by virtue of the “one member, one vote” rule;
- cooperatives at other levels are also organized in a democratic manner.

#### **3rd Principle: Member economic participation**

- Members contribute equitably to, and democratically control, the capital of their cooperative.
- At least part of that capital is usually the common property of the cooperative.

- Members usually receive limited compensation, if any, on capital subscribed as a condition of membership.
- Members allocate surpluses for any or all of the following purposes:
  - ❖ developing their cooperative, possibly by setting up reserves, part of which at least would be indivisible;
  - ❖ rewarding members in proportion to their transactions with the cooperative; and
  - ❖ supporting other activities approved by the membership.

#### **4th Principle: Autonomy and independence**

- Cooperatives are autonomous, self-help organizations controlled by their members.
- If they enter into agreements with other organizations, including governments, or raise capital from external sources, they do so on terms that ensure democratic control by their members and maintain their cooperative autonomy.

#### **5th Principle: Education, training and information**

- Cooperatives provide education and training for their
  - ❖ members,
  - ❖ Elected representatives,
  - ❖ managers and
  - ❖ employees
- so that they can contribute effectively to the development of their cooperatives.
- They inform the general public, particularly young people and opinion leaders, about the nature and benefits of cooperation.

#### **6th Principle: Cooperation among cooperatives**

- Cooperatives serve their members most effectively and strengthen the cooperative movement by working together through
  - ❖ local,
  - ❖ national,
  - ❖ regional and
  - ❖ international structures.

#### **7th Principle: Concern for community**

- Cooperatives work for the sustainable development of their communities through policies approved by their members.



## Chapter 4: Types of Cooperatives

- Cooperatives operate in all sectors of the economy
- it is difficult to list them for each sector.
- Base of our criterion the **two** principal objective of the members .
  1. Service cooperatives, and
  2. Worker Cooperatives. their goal is to get a job (i.e. producer and labor cooperatives)
- This distinction will then allow us to evaluate the importance of cooperatives in the world.

### I. Service Cooperatives

- In these cooperatives, the members join together with a view to enjoy economic advantages by securing the goods and services they need to exist.

Service cooperatives can be made up of natural persons or corporate bodies.

- 4.1. Financial cooperatives
- 4.2. Consumer Cooperatives
- 4.3. Farmers' or Agricultural cooperatives
- 4.4. Housing cooperatives
- 4.5. Public service provision cooperatives

#### 4.1. Financial cooperatives

- this cooperatives” covers credit unions and insurance cooperatives.
- Offers financial services such as savings and loans at favourable interest rates and insurance services.

the case of financial cooperative in Senegal.
- The credit union of the artisans / skilled craftsperson
- It was formed in 1999 and has been operating since January 2000.
- Its object is to meet the financial needs of the artisans through savings and loans, in all the urban and rural parts of the Thiès region.
- This cooperative is composed of three constituent bodies, namely:
  - The seven-member credit committee which receives and considers loan applications;
  - The seven-member supervisory committee whose job is to monitor working practices and the integrity of management; and

- A thirteen member education and training committee which takes care of member training activities.
- From 402 members at the beginning with savings of 4 million CFA francs, the cooperative has grown to 910 members today with savings of 54.6 million CFA francs.
- Most of its members are artisans and joined on an individual basis or through a business.

#### **4.2. Consumer Cooperatives**

Their main object is to supply their members with goods and services for their personal use at the lowest cost

They are to be found in different sectors such as:

- -food;
- -housing;
- -educational goods and services;
- -leisure.

It has been used above all in the food sector both:

- in developing countries struggling against insecurities of food supply and
- in industrialized countries in the grip of unstoppable rises in the cost of consumer goods.

The member/consumer enjoys quality goods and services at minimum cost.

Grain banks have also played a major role in the self-sufficiency in foodstuffs of several developing countries.

These banks have a double function. On the one hand they supply people with food, and on the other they allow their members to secure enough money to let them buy produce from different regions. Members can be sure that their cooperative is listening to their needs because they take part in the decision making.

Case of Japan:

- Although it was formed in 1965 by “ordinary“ housewives, the Seikatsu Club Consumers’ Cooperative Union (SC) in Japan is not a consumer cooperative like others.
- It all started when a housewife organized 200 women to buy 300 bottles of milk so as to reduce the price.

- The cooperative that has since developed puts the emphasis on the direct producer/consumer relationship to moderate and humanize the market. The cooperative works on the basis of two rules:
  - democratic and
  - autonomous management encouraging all the members to participate, and maintaining a close relationship between SC members and the producers.
- Since 1965, the SC has devoted itself to the environment, to women's rights and to improving their working conditions. It is so successful that it has managed to have had more than 100 of its members elected to various political positions. More and more women in Japan are entering the workplace, and the SC has therefore put in place cooperatives of female workers to undertake distribution and other services such as recycling, a child-care service, an insurance company, etc. There are at present more than 200 organizations and 8,000 female workers.

#### **4.3. Farmers' or Agricultural cooperatives**

- Agricultural cooperatives help growers:
  - with the marketing of their harvest by obtaining consumer goods and input
  - helping with the management of farming credit.
  - By reducing the number of middlemen, producers are in a position to conclude a much better deal with traders or
  - contract with any buyer they like.

#### Case of Benin

- The cooperative association for rural development of Banikoara in Benin (ACOODER) is one of several examples of cooperation among agricultural producers.
- Formed in 1971, it helps them in
  - supply of farming materials for, and
  - marketing of farm produce.
- Today it has limited its field of operations to representing and defending the interests of farmers
- providing financial, technical and training services for them as well as for cooperative organizations.
- it also sells the cotton produced by local growers.

- In 1998 it combined 71 cooperative organizations bringing together about 11,000 members.

#### **4.4. Housing cooperatives**

- come together to secure decent housing.
- Housing cooperatives are thus trying to respond to their members' needs regarding access to affordable good quality housing, security of tenure and a safe community to live in.
- They offer the best possible service at an equitable price, the lowest possible.
- In more practical terms, the residents/owners of the block, jointly take upon themselves the entire management of their building and the cooperative itself.
- Therefore it is usually in a position to charge much lower rent than the market rate.
- Also, this involvement of everyone is explicitly recognized by several cooperatives which offer their members a "member's contract" comprising a reduction in the rent stated in the signed lease.
- Thus a resident who systematically refuses to carry out tasks could lose his status as a member and have to pay the rent set in the lease.

Advantages of the housing cooperative:

- ✓ a quality home at a good price,
- ✓ long term loan
- ✓ security of tenure,
- ✓ control of one's environment,
- ✓ involvement in the running of the cooperative.

The case of Kenya

- The National Cooperative Housing Union (NACHU) is an organization that has existed in Kenya since 1979.
- It is run by a Board of Directors composed of one representative from each of the 8 Kenyan provinces and 3 administrators elected so as to ensure a better male-female representation.
- It comprises 214 housing cooperatives sheltering about 200,000 people.
- The housing cooperatives in Kenya are construction cooperatives where the members become owners both of their plot of land and of their building.
- However the cooperative provides collective services such as communal toilets.

#### 4.5. Public service provision cooperatives

- The provision of services considered to be in the “public” interest like electricity or water supply, communication and transport.
- In developing and transitional countries for example, when the State takes charge of these services, they are often badly run, costly and of bad quality.
- In developed countries, the State sometimes leaves the provision of such services to private companies.
- But these capitalist companies, out to make maximum profits, set prices which rarely reflect the quality of the service they sell.
- It must be said that the cooperative form of organization possesses features that predispose it to the supply of public services:
- The cooperative leaves the control of the service to its users and guarantees that the product or services meet the users’ needs;
- The mandate of the cooperative is both social and economic.
- This corresponds to the main function of the public sector which is to balance socio-economic development with the best expectations/ interests of the public;
- In practice, the provision of public services by cooperatives is not at all new. It has been happening for some years now in Argentina, Canada, the USA and Finland and is starting in a growing number of countries.
- In the United States, rural electricity supply cooperatives run more than half of the electricity lines, carrying power to more than 25 million people in 46 States.
- Public service cooperatives have existed for several years in all regions of Canada and supply households with electricity, gas, telephone services, sewage/ dirt and water supply services, fire-fighting services, etc.
- In this field more than 400 cooperatives offer services to about 150,000 households. For example,
  - a group of individuals can decide to form an electricity cooperative in order to secure relief from the frequent power cuts affecting their town.
  - Of course, the cooperative cannot serve only its members; nevertheless its primary aim being to meet the electricity supply needs of its members,
  - it is by the “domino effect” that it will improve the living conditions of non-members.

- It is interesting to note that there is no contradiction at all with the seventh cooperative principle of concern for community.
  - In France, a new type of cooperative has appeared: La Société coopérative 'intérêt collectif' (SCIC) or community interest cooperative society.
- This form of cooperative has the objective of producing or supplying goods or services in the community interest which are socially useful in nature:
- help in the home, integration through economic activity, socio-educational activities, tourism, etc.
  - The title of social usefulness lets the coop enjoy tax breaks.
    - At the same time the United Kingdom is about to create a new form of enterprise equivalent to the SCIC, "Community Interest Companies".  
Shared services cooperatives or support services cooperatives.
    - A shared services or support services cooperative is a cooperative whose members are private companies or public bodies which together acquire goods and/or services of an assured quality at the best possible price.
- In the United States, VHA is a cooperative whose members are:
    1. 2,200 health care institutions based in their community representing 26% of all the community health institutions in the United States and
    2. about 175,000 independent doctors.
  - VHA was founded in 1977 by 30 health care institutions.
  - The main goal was to compete with private hospitals by a united effort to acquire communal goods and services.
  - Each year VHA negotiates for more than 17 billion US dollars worth of supply contracts for its members.
  - In 2000, VHA members earned 1.15 billion US dollars in refunds, savings and additional holdings, being a return on investment of 56 to 1.
  - In other words. VHA members save or receive more than \$56 for each dollar paid in subscription charges to VHA.

## **II. Worker cooperatives**

- Its main objective is to create jobs for members.
- There are two categories of worker cooperatives:

1. producer cooperatives and
2. labor cooperatives.

#### **4.6. Producer cooperatives**

- are both co-owners and employees of the cooperative whose aim is to produce and sell goods and/or services.
- The employees together decide on the general direction and appoint their leaders (manager, administrators, etc.)
- They also decide how to divide up any surplus.
- Another novelty of this type of cooperative is that it allows for the takeover and restart of a bankrupt business.
- This option is one way of keeping going and developing the business and existing jobs.

#### **4.7. Labor cooperatives**

- They sell their labor and skills to other enterprises.
- They generally operate in the fields of packing and maintenance of highways and public buildings, etc.

#### Case of Canada

- In Canada the FCCT, or Canadian federation of worker cooperatives, was constituted in 1992 to act as an “umbrella” organization for the numerous worker coops in the country.
- The , FCCT’s vision is :
  - to develop and sustain an integrated network of democratic worker coops
  - which offer great quality of life at work and which consult with each other to support sustainable local economies.
- Often the members of this coops are from the working class, without a job and are not entrepreneurs.
- the coop has a mandate to exert pressure on governments to enable members of worker coops to participate in different government programmes.
- At the present time, the FCCT is very busy in the rural Atlantic Provinces of Canada where the unemployment rate is very high.
- The Federation is doing its best to breathe new life into the Atlantic Provinces and to re-launch industry in that very needy part of Canada.

Agricultural cooperatives: the largest number of members

- Agricultural cooperatives enjoy success both in industrialized and in developing countries.
- “Agricultural cooperation” makes up the largest cooperative movement in the world in terms of the number of members.
- At present more than 410 million members in 540,000 cooperatives.
- Asia has more than 83% (448,200 coop) of the total number of cooperators (situated mainly in India and China).
- But in terms of turnover, Europe is in top spot (thanks to French, German, Dutch and Italian cooperatives) with 42% of the total turnover, amounting to more than 600 billion dollar
- In Europe there are 44,260 cooperatives with 14 million members and 720,000 jobs.  
In 2000, the American agricultural cooperative:
  - 3,346 cooperatives.
  - turnover amounts to 99 billion dollars (6.9%) .

In developing or transitional countries, although this type of coop is an assured source of national income, the withdrawal of the State from the sector and liberalization of economies have weakened the movement but it is nevertheless still there.

- In 2001 the agricultural cooperatives of Kenya had a turnover /income of 100.6 million dollars.

New features in cooperative affairs

The novel and even innovative applications in industrialized countries:

- -Cooperatives were the first enterprises to think about Centers of Business Development in the field of federations/collective of services to cooperatives;  
-Collective service cooperatives:
  - where rural electricity cooperatives, have existed for a long time in the US America and also being developed in Portugal.
  - In the United Kingdom, a telephone cooperative has recently been set up with excellent results:
    - it buys “communication time” at advantageous rates and passes on the savings to its members in the form of reduced cost or payment of dividends,



- -Social cooperatives set up in Italy and central Europe provide lots of jobs for :
  - handicapped members
  - former detainees / prisoners and
  - drug addicts;
- Franchising cooperatives : A franchise is a contract whereby one enterprise (the franchiser) allows one or more independent businesses (the franchisees), in return for a fee, the right to use its trade name and logo to sell products or services.
  - are being developed in the United States , in Europe
  - The creation of sub-contractors cooperatives of the large Japanese car manufacturers gave small sub-contractors greater power of negotiation and meant they could avoid breaks in supply;
- “campus cooperatives” In the United States and Japan, offer students numerous services, such as low-cost shops, accommodation, and counseling services.
  - The student cooperative of Harvard Business School in Boston in the United States and
  - the Higher Pan African Institute of Cooperative Economy of Cotonou in Benin are a couple of the best-known examples;

## **Chapter 5: Cooperatives laws**

### **5.1. Definition and concepts of cooperatives law/legislation**

#### **Pre test**

Cooperatives as business organizations need to have laws and bylaws according to their nature? Why? Reflect your own suggestion?-----

- Legislation is the word for all the laws and legislative measures of a country.
- It is the most appropriate way of controlling the activities of people working in the field of economics
- Coop legislation helps:
  - regulate the activities of coop,
  - to define ways of setting up a cooperative,

- its operating practices, etc.

Coop legislation takes different forms depending on the country:

1. Those adopt a single law applicable and valid for all coop (Germany, Brazil, Côte d'Ivoire, Thailand, Mexico]among others);
  2. Others have specific laws for a given type or sector of coop separately (Ethiopia, Japan, France, Rumania among others);
  3. In some countries, cooperatives are regulated by specific chapters of more general codes like the Civil Code or the Commercial Code (Switzerland, Belgium among others);
  4. Coop can also be regulated by special provisions governing the application of a more general law to cooperatives (the United Kingdom for example).
  5. Some countries like Denmark and Norway have the distinction of not having any cooperative legislation
- In spite of their diversity , all legislation on cooperatives is usually in three parts.
  - First of all, a law, an ordinance, a decree, a proclamation or a decision, whatever is the term used for it in the country in question, sets forth the fundamental nature and the general principles.
  - Secondly, regulations drawn up to conform to the law are issued
  - Thirdly and finally, the rules governing their operating procedures are set.
- Cooperative legislation evolves differently according to the region.
- In industrialized countries:
    - the influence of cooperatives in the economy can prove considerable depending on the sector, legislation helps cooperatives to secure finance on the capital markets while limiting access to the right to vote of non-members, out of respect for the cooperative principle of autonomy and independence.
  - In countries in transition,
    - the passage from a planned economy to a market economy has serious consequences for the countries of Central and Eastern Europe.
    - Before the collapse of the socialist system, coops had to conform to the centralized economic plan, drawn up by the State.
    - Following the fall of socialism, legislation in these countries tried very hard to confer the status of private enterprise on cooperatives.

- In developing countries,
  - Economic liberalization, globalization and programmes of structural change have contributed to lessening / reduction the stranglehold / Monopoly of the State on cooperatives.
  - Legal bills/ a written proposal for a new law have tried to follow this evolution, sometimes with some success mainly in Asia (Malaysia, Mongolia, Nepal, Thailand, Vietnam).
  - After the complete expropriation/ Appropriateness of the cooperative movement by the State, the legal bills of developing countries are doing their best to give cooperatives autonomy and independence.

### **Content of a cooperative law**

Preamble: Defines guidelines for interpretation of the law.

General provisions: This section contains, among other matters, the definition of a cooperative society, the cooperative principles, a definition of terms used in the law...etc.

Formation, registration and publication:

- Formation (status of members, their number, age restrictions).
- This section also contains guidelines for the procedure for registering the cooperative with the competent authorities and its consequences as well as
- for the rules for admission and resignation of members and
- conditions for their exclusion and suspension.

Obligations and rights of members:

Organs and management of the cooperative society:

- A list of the different organs of the cooperative along with their composition and powers is drawn up (General Meeting, Board of Directors, and Supervisory Committee).

### **Funding, accounts and distribution of surpluses:**

- the cooperative's internal and external financial resources
- a definition and description of a share, the reserve fund,
- ways of distributing the surplus at the end of the financial year

Audit:

- procedure for controlling the accountability and management of an enterprise and the way it fulfills its objectives.
- It monitors whether the interests of third parties, administrators and members are being protected.
- The audit can be internal or external
- The frequency of internal and external audits must be clearly defined in the law.

Forms of dissolution/ termination:

- The law deals both with the steps to take
  - after dissolutions without liquidation / Bankruptcy and
  - dissolutions with liquidation.
- Simplified structures: The law might provide organization less complex than the traditional cooperative.
- Apex organizations: The cooperative law has to define the roles of unions,
- Settlement of disputes: The cooperative law specifies the way disputes in cooperative matters are dealt with and settled.
- Miscellaneous, transitory and final provisions:
- The legal penalties incurred by particular acts and on the decree specifying how the law should be enforced, etc.

## **5.2. By-Law of Cooperative Society**

Every Society shall have its own by-laws.

The contents of the by-law shall include the following issues:

- Name and address of the society
- Objectives and activities of the society
- Working place or area of the society
- Requirements necessary for membership of the society
- The rights and duties of members of the society
- The powers, responsibilities and duties of the management bodies
- Conditions for withdrawals and dismissal from membership
- Conditions for re-elections, appointments, term of office and suspension or dismissal of the members of the management committee or other management bodies.

- Conditions for calling of meeting and voting of the society.
- Allocation and distribution of profit
- Auditing
- Employments of workers
- Other issues not contrary to this proclamation
- By-laws of a society may be amended by the special resolution of the general assembly.
- However, the amendment shall be effective on the date of its submission to and registration by the appropriate authority.
- Where the society decides on the amendments of its by-laws three copies of the amendment and the special resolution of the society made in accordance with this proclamation shall be submitted to the appropriate authorities within 30 days from the date of decision.
- The appropriate authority shall register the amendment and give evidence of its registration to the society
- Where it is satisfied that the amendment of the by-laws was made in accordance with this proclamations and regulations issued for the implementation of this proclamation.

### **5.3. Ethiopian cooperatives societies' proclamation**

- Cooperative societies after the market reform.
- Two proclamations have been issued regarding cooperative societies.
  - The first one is proclamations No. 85/1995 and
  - The second one is proclamations No. 147/1998.
- Both are similar in contents but deferent in types of cooperative societies proclaimed to be established.
- Currently, proclamations No. 147/1998 is functional.
- The proclamation has 10 parts and 60 sections.

#### **PART I GENERAL (5 sections)**

- **Section 1. Short Title.** This Proclamation may be cited as the “Cooperative societies, Proclamation No. 147/1998.”
- **Section 2. Definitions.** In this Proclamation unless the context otherwise requires:
  - 1) "Society" means a cooperative society established and registered in accordance with this Proclamation and

it shall in particular include the following:

- (a) Agricultural Cooperative Societies;
  - (b) Housing Cooperative Societies;
  - (c) Industrial and Artisans Producers' Cooperative Societies;
  - (d) Consumers Cooperative Societies;
  - (e) Savings and credit Cooperative societies;
  - (f) Fishery Cooperative Societies;
  - (g) Mining Cooperative Societies;
- 2) "Cooperative Society" means a society established by individuals on voluntary basis to collectively solve their economic and social problems and to democratically manage same;
- 3) "Member" means any physical person, or society established under this proclamation which is registered after fulfilling his membership obligations.
- 4) "General Assembly" means a meeting of members of the Primary Cooperative society or representatives of societies above primary level;
- 5) "Special resolution" means a resolution passed by a two third majority of the members to be binding on all members;
- 6) "Management Committee" means a body elected and empowered by the general assembly with the responsibility to manage the activities of the society;
- 7) "Appropriate Authority" means an organ established at deferent level,
- to organize and register cooperative societies and
  - to give training,
  - conduct research and provide other technical assistance to cooperative societies;
- 8) "Person" means a natural or juridical person.

**Section 3.** Where the provisions of the Proclamation are set out in the masculine gender they apply equally to the feminine gender.

**Section 4.** Objectives of a Society. The society have one or more of the following objectives:

- 1) To solve problems collectively which members cannot individually achieve;
- 2) To achieve a better result by coordinating their knowledge, wealth and labour;
- 3) To promote self-reliance among members;

- 4) To collectively protect, withstand and solve economic problems;
- 5) To improve the living standards of members by reducing production and service costs;
- 6) To expand the mechanism by which technical knowledge could be put in to practice;
- 7) To develop and promote savings and credit services;
- 8) To minimize and reduce the individual impact of risks and uncertainties;
- 9) to develop the social and economic culture of the members through education and training.

### **Section 5. Guiding Principles of Co-operative Societies. Co-operative societies :**

- 1) are voluntary organizations open to all persons without any discrimination.
- 2) democratic organizations controlled, equal voting rights and accordingly one member shall have one vote.
- 3) receive dividends from profit according to their shares and contribution.
- 4) are autonomous self help organizations controlled by their members.
- 5) provide education and training for their members, elected representatives, managers and employees
- 6) serve their members most effectively and strengthen the society's movement by working together through local, national, regional and international structures.
- 7) work for the sustainable development of their communities through policies approved by their members.

### **Part II: Formation and Registration of the Societies**

#### **Section 6. Formation of Co-operative Societies.**

- 1) Co-operative societies may, according to their nature, be established at different levels from primary up to the federal level.
- 2) A primary society shall be established by persons who live or work within a given area.
- 3) The number of members in a primary society to be established shall not be less than ten /10.
- 4) Notwithstanding Sub-Article (2) of this Article, the appropriate authority may specify in the directive, the minimum number of members that could make a society economically feasible.

5) A society may sell one of its shares to persons outside its area when the society faces shortage of capital.

### **Section 7. Types of Societies.**

- 1) A society may engage in either production or service rendering activities or in both.
- 2) The field of activities to be engaged in by any society shall be determined by the by-laws of the society.

### **Section 8. Name of a Society.**

- 1) Any society shall have its own name
- 2) Words "Cooperative Society and Limited Liability" shall appear in the name of every society.
- 3) A name or distinguishing mark registered by one society shall not be used by any other society.
- 4) The name of every society shall be written boldly and be put at every place where the society's activities are performed.

### **Section 9. Registration of a Co-operative Society.**

- 1) Any society shall be registered by the appropriate authority.
- 2) Any society, when established shall submit an application for registration together with the following particulars to the appropriate authority:
  - (a) Minutes of the founders meeting;
  - (b) The by-laws of the society in, three copies;
  - (c) Names, address and signature of the members;
  - (d) Name, address and signature of the members of the management committee of the society;
  - (e) A detailed description which proves that the registered members of the society have met the
  - (g) Plan of the society;
  - (h) Documents showing that the amount of capital of the society and the capital has been collected and deposited in a bank account, if there is no bank in the area, that it has been deposited in a place where the appropriate authority has designated;
- (i) The description of the land on which the society operates;



(j) Other particulars that may be specified in the regulations or directives issued for the implementation of this Proclamation.

3) The appropriate authority shall register a society and issue a certificate of registration within 15 days

4) When the appropriate authority rejects the application for the registration of a society, it shall give a written explanation to the representatives of the society within 15 days.

### **Section 10. Juridical Personality and Responsibility.**

1) Any society registered in pursuance of Article 9 of this Proclamation shall have juridical personality from the date of its registration.

2) Any society shall not be liable beyond its total asset. It has limited liability.

### **Section 11. By-laws of Society.**

1) Every society shall have its own by-laws.

2) The contents of the by-laws shall include the following particulars:

(a) Name and address of the society;

(b) objectives and activities of the society;

(c) working place (area) of the society;

(d) Requirements necessary for membership of the society;

(e) The rights and duties of members of the society;

(f) The powers, responsibilities, and duties of management bodies;

(g) conditions for withdrawal and dismissal from membership;

(h) Conditions for re-election, appointment, term of office and suspension or dismissal of the members of the management committee or other management bodies;

(i) meeting and voting of the society;

(j) Allocation and distribution of profit;

(k) Auditing;

(l) employment of workers;

(m) others

3) By-laws of a society maybe amended by the special resolution of the general assembly.

4) three copies of the amendment and the special resolution of the society made in accordance with this Proclamation shall be submitted to the appropriate authority within 30 days from the date of the decision.

### **Section 12. Amalgamation and Division of Societies**

1) a new society may be formed :

- (a) by dividing itself into two or more societies; or
- (b) by amalgamating / merging itself with one or more societies.

2) The special resolution on the amalgamation or division needs:

- a) full agreement of the members, creditors and the appropriate authority
- 3) The previous registration of societies shall be canceled
- 4) The rights and duties of societies which have lost their identities by amalgamation shall be transferred to the newly formed society.

## **PART III: THE RIGHTS AND DUTIES OF MEMBERS OF A SOCIETY**

### **Section 13. Necessary for Membership of a Society.**

example, age limit 18 years for secondary, 14 for primary coop, he is able to pay the share, registered with the appropriate authority

### **Section 14. Rights and Duties of Members.**

#### **14.1) Rights:**

- (a) to obtain services and benefits according to his participation
- (b) to participate in the meetings of the society and to vote;
- (c) to elect and be elected;
- (d) to withdraw from the society on his request with payment of benefits.

#### **14.2) duties:**

- (a) to respect the by-laws
- (b) to implement the by-laws and directives of the society;
- (c) to pay for share of capital and registration fee;
- (d) to protect the common property of the society.

### **Section 15. Dismissal from Membership.**

- 1) on his own initiative;
- 2) because of committing repeated faults;

- 3) The rights of any dismissed member shall be respected in accordance with the by-laws of the society;
- 4) any dismissed person with Sub- Article (1) may reapply for membership.

#### **Section 16. Payment of Shares.**

- 1) The capital which enables the society to expand its work activities shall be obtained from paid up shares of each member
- 2) The society may sell additional shares if it is found necessary to promote the financial capacity with the decision of the general assembly;
- 3) No member shall hold more than 10% of the total paid up share capital...

#### **Section 17. Register of Members.**

Every society shall keep a register wherein shall be entered:

- 1) the name, address, occupation, age and sex of each member;
- 2) the date on which he became a member;
- 3) the amount of shares held and the registration fee paid;
- 4) the name and address of the heir of the member;
- 5) any other particulars that may be specified in the by-laws.

#### **Section 18. Voting.**

- 1) regardless of the number of shares he has, have only one vote at the meeting of the society;
- 2) Every member in a primary society shall personally be present at the meeting of the society to cast a vote;
- 3) Members of a society above primary level shall cast a vote through their representatives.

#### **Section 19. Transfer of Share or Benefit.**

- 1) No transfer by a member of his share or benefit in a society shall be valid unless:
  - (a) the member has held such share or benefit for at least one year before he transfers;
  - (b) the transfer is approved by the management committee.
- 2) On the death .. transferred to one of his heirs designated
  - 3) Where such heir is not a member and does not wish to become ,

- 4) he shall be paid the value of the share;
- 5) The transfer or payment concluded in pursuance of Sub-Article (2) of this Article shall not be reversed due to the claims paused by third parties on the society.

**Section 20. Supreme Organ of a Society.** The supreme organ of any society shall be the general assembly.

#### **PART IV: MANAGEMENT BODIES**

1. The General Assembly
  2. Management Committee.
  3. Control Committee (Audit and Inspection)
  4. Other Sub-Committees.

#### **Section 21. Powers and Duties of the General Assembly (GA).**

- Pass different decisions;
- approve and amend the by-laws and internal regulations of the society;
- elect and dismiss the members of the deferent committees,
- determine the amount of shares ;
- decide on how the annual net profit of the society is distributed;
- hear work reports and give proper decision;
- decide that a society either be amalgamated or be divided
- approve the annual work plan and budget;
- Decide any issue submitted by the management committee and other committees.

#### **Section 22. Calling of General Assembly.**

- 1) at least once in a year;
- 2) If the management committee or one third of the members agree.

#### **Section 23. Management Committee.**

- 1) Every society shall have a management committee
- 2) The term of office of the management committee shall be three years.
- 3) not be elected for more than two consecutive terms. They may be dismissed at any time by the general assembly.

**Section 24. The powers and duties of the management committee:** include the following:

- 1) maintain the minutes of a meeting in writing;

- 2) maintain the documents and books of accounts of the society;
- 3) prepare the annual work programme and budget of the society; implement same upon approval;
- 4) call general assembly
- 5) execute such other decisions given by the general assembly;
- 6) submit reports to the general assembly on the activities of the society.

### **Section 25. Control Committee.**

- 1) is accountable to the general assembly and the number of which shall be specified by the by-laws of the society;
- 2) The term of office of members of the committee shall be three years.  
No members of the control committee shall be elected for more than two consecutive terms

### **Section 26. Powers and Duties of the Control Committee.**

- 1) follows up that the management committee is carrying out its responsibilities properly;
- 2) follows up that the funds and property of the society are properly utilized;
- 3) controls that the various activities of the society are carried
- 4) performs other duties given by the general assembly (GA).

### **Section 27. Other Sub-Committees.**

- Other sub-committees may be established pursuant to the by-laws of the society.

## **PART V: SPECIAL PRIVILEGES OF SOCIETY**

### ***Section 28 - 30***

- Priority of claims by Society.
  - debts owed to the society by member shall take precedence over all other debts, except the debt owed to the Government.
  - Set-off /counterbalances in respect of Share or Benefit of Members. Benefits ← commensurate → debts
  - The shares or benefits of any member may be set-off for debts due to the society from such a member.
- **Section 31. Government Assistance.**

- 1) societies which are organized and registered under this Proclamation shall be entitled to the following:
  - a) to be exempted from income tax; provided however, members shall pay income tax on their dividends;
  - (b) to acquire land as determined by the nearby Government;
  - (c) to receive other assistance from the nearby Government.
- 2) rendering man-power training and conducting studies and research shall be established.

## **PART VI: ASSET AND FUNDS of the SOCIETIES**

### **Section 32. Indivisibility of Asset and Funds of a Society.**

- the asset and fund of a society shall not be divided for the members or any other party.

### **Section 33. Allocation of Net Profit.**

1) The society shall deduct 30% of the net profit obtained and allocate for the following purposes;

- (a) for reserve;
- (b) for the expansion of work;
- (c) for social services.

2) After the amount prescribed in Sub-Article (1) is deducted the remaining net profit shall be divided among the members; the division shall be made on the basis of:

- the shares and
- on the amount of goods offered for the sale to the society or
- goods purchased from the society by members of the society.
- **Section 34. Restrictions on Borrowings.**
- 1) A society ***shall receive loans*** from its members or other organizations ---- specified in *the by-laws of the society*.
- 2) Interest on loans received from its members ***shall not exceed the current interest rate of a bank***.
- **Section 35. Restrictions on Loans.**
- A society ***shall not extend*** loans other than to its members

## **PART VII AUDIT AND INSPECTION**

**Section 36. Audit.**

- 1) The appropriate authority shall audit or causes to be audited at least once in a year.
- 2) The audit shall include the examination and verification of:
  - overdue debts, if any, and
  - cash balance,
  - securities and assets, and liabilities.
- 3) The audit report shall be submitted to the general assembly.

**Section 37. Inspection.**

- 1) The appropriate authority assign the person to inspection to the organization, work execution, documents and financial condition of a society.
- 2) Without prejudice to Sub-Article (I) of this Article inspection may be made when:
  - (a) a majority/ not less than one-third of the members of the executive committee request;

**Section 38. Keeping Audit and Inspection Results.**

- shall be kept in the office of the authority and the society, open and easily accessible to everyone.

**Section 39. Actions to be Taken for Losses of Property or Fund of the Society.**

- 1) The auditor or inspector shall make a report to the management committee or the general assembly or the appropriate authority,

The committed problem may be the :

  - (a) Any payment contrary to the by-laws;
  - (b) any damages to the assets of the society
    - (a) misappropriated the properties of the society.
- 2) The appropriate authority who received the report shall give the person concerned an opportunity to present his defense within fifteen days.
- 3) After fulfillment of the above mentioned conditions,
  - the person who has been found responsible for misappropriation of the fund or property of the society to return or pay same with interest including compensation and damages.
  - Where the person concerned is not willing to do so, the authority shall take the appropriate legal measure.

## **PART VIII DISSOLUTION/TERMINATION AND WINDING UP OF SOCIETIES**

### **Section 40. Dissolution of a Society.**

A society shall be dissolved on the following grounds:

- 1) Where a special resolution for its dissolution is given by the members; or
  - 2) where the number of members of a primary society falls below ten.
- a society the dissolution of which is decided shall notify same to the appropriate Authority within seven days from the decision for its dissolution.

### **Section 41. Liquidator. (RESPONSIBLE FOR THE PROCESS OF DISSOLUTION)**

- 1) the appropriate authority may assign a liquidator. It may, if necessary, determine that his remuneration be paid out of the accounts of the society.
- 2) The liquidator shall receive records, documents and properties of the society as soon as he is assigned.

He shall also take the necessary measures to protect the properties and rights, records and documents of the society from damages.

### **Section 42. Powers and Duties of the Liquidator.**

1) He shall in particular perform the following in order to carry out his duties properly:

- (a) investigate all claims against the society
- (b) collect the assets of the society;
- (c) distribute the assets in accordance with the plan of liquidation approved by the general meeting of the society;
- (d) carry on the work activities of the society
- (e) represent the society in legal proceedings;
- (f) call meetings of the members as may be

2) He shall issue notice in a newspaper, before the distribution of property of the society , It shall proceed with the distribution where no claim is presented within two months from the date of such notice.

3) Upon completion of the winding up proceedings the liquidator shall prepare and submit a report to the appropriate authority;

he shall deposit the records and documents of the society in such places as the appropriate authority may direct.

### **Section 43. Calling on Creditors.**



- 1) Creditors shall be paid on the basis of a balance sheet prepared by the liquidator.
- 2) Creditors shall be informed of the dissolution of the society and required to file their claims with supporting documents.
- 3) Creditors appearing in the society's records or who are otherwise known shall be notified directly by registered letter.

#### **Section 44. Protection of Creditors.**

- 1) Until the creditors of the society have been paid or amounts required for payment be deposited, the liquidators may not distribute any part of assets among the members.
- 2) Where known creditors have failed to present their supporting documents, the amounts owing to them shall be deposited according to the decision of the court.
- 3) unless the creditors are guaranteed or distribution of assets is postponed until such undertakings are completed.
- 4) After the payment of claims have been completed , the liquidators may distribute the assets of the society among the members based on the amount due to them.

#### **Section 45. Cancellation of a society from the Register.**

- the certificate of registration shall be returned to the appropriate authority

### **PART IX : SETTLEMENT OF DISPUTES**

#### **Section 46. Conciliation.**

The disputes shall be heard by a third party appointed by the disputing parties before they are referred to the arbitrators.

#### **Section 47. Arbitration.**

- 1) when not settled by conciliation they shall be referred to arbitration.
- 2) The arbitration shall consist of three persons of high reputation and impartiality.
- 3) The arbitrators shall conduct their hearing and fulfill any of their duties in accordance with the Civil Procedure Code.

#### **Section 48. Appointment of the Arbitrators.**

- 1) Each party to the dispute shall appoint one arbitrator. The third arbitrator, who shall be the chairperson, shall be appointed by both parties.
- 2) The appropriate authority shall appoint the chairperson arbitrator when the parties fail to reach an agreement.

**Section 49. Disputes to be referred to Arbitration.**

- The arbitrators shall have the power to hear disputes not settled by conciliation regarding
  - the organization,
  - management, or
  - operations of a society which arises between:
    - 1) members and members
    - 2) members and any the management committee
    - 3) the society or the management committee and any former management committee

**Section 50. Civil Court Powers of Arbitrators.**

- The Arbitrators shall have the same power as a Civil Court
  - for the summoning of witnesses, ➔ production of evidence, ➔ the issuing of orders or ➔ the taking of any legal measures.

**Section 51. Execution.**

- Any decision, order or award made under this Proclamations shall be taken as though made by a civil court, and, where appropriate, the courts shall have jurisdiction to order the enforcement of any such decision, order or award.

**Section 52. Power of Courts.**

- Appeals / request on the decisions given by the Arbitrators may, as the case may be, be instituted in Federal High Court, or the Regional State High Court or the Federal High Court of a city accountable to the Federal Government where the society is situated.

**PART X: MISCELLANEOUS PROVISIONS****Section 53. Address of a Society.**

- Any society shall have an address registered
- All services of process, notices and other communications shall be sent in such address.
- The society shall inform the appropriate authority of any change in such address within thirty days.

**Section 54. Supplying Information.**

- Every society shall have the obligation to transmit information to the appropriate authority about the activities it performs.

#### **Section 55. Establishment of a Federal Organ.**

- A Federal Organ responsible for organizing and registering Apex organizations and for rendering training, conducting research and other technical support to societies may be established by law.

#### **Section 56.**

- Depositing of this Proclamation, Regulations and the By-laws.
- Every society shall deposit at its address copies of this Proclamation, the Regulations and the by-laws to be accessible free of charge.

#### **Section 57. Repealed and Inapplicable Laws.**

- No law, regulation or directive in. so far as it is inconsistent with this Proclamation have force or effect in respect of matters provided for by this Proclamation.

- **Section 58. Transitory Provisions.**

- The cooperative societies which have been established and operating in accordance with Proclamation No.138/1978 shall be reorganized under this Proclamation.
- The cooperative societies which have been established and operating in accordance with Proclamation No. 85/1995 shall be deemed to have been established under this Proclamation and shall continue to carry out their functions in accordance with this Proclamation.
- The societies indicated in Sub-Article (1) of this Article shall continue their operations holding their previous juridical personalities until they are reorganized and registered by the appropriate authority.
- The appropriate authority shall facilitate the conditions necessary for the reorganization of the societies in accordance with sub-Article (1) of this Article.
- **Section 59. Issuance of Implementing Legislations.**
- The Council of Ministers of the Federal Government or the appropriate organ of a Region or city accountable to the Federal Government may issue legislations for the proper implementation of this Proclamation.

#### **Section 60. Effective Date.**

- This Proclamation shall come into force as of the 29th day of December, 1998.

- for the last 17 years.

### **Self-test**

1. Discuss on the first Ethiopian cooperative legislation of 1960: its strengths and drawbacks.
2. What is the theme of 2002 Cooperatives' Commission Establishment Proclamation (No. 274/2002)?
3. Explain the compliance of Ethiopian cooperatives legislations (and their amendments) with Ethiopian development plans (strategies).

## **Chapter 6: Organization and management of cooperatives**

### **6.1. Procedures for organizing cooperatives**

- This setting up process can be broken down into six steps:
  1. Form a core group
  - 2: Carrying out a feasibility study
  3. Drawing up a business plan
  4. Organizing the inaugural general meeting
  5. Applying for registration and/or consent for the cooperatives
  6. Getting the cooperative started

#### **Step no.1: Form a core group**

- The inspiration / ideas for the creation of a cooperative generally comes from one or several people who have known of the potential for the set up of a cooperative and who have a good idea and a vision.
- The idea can also come from a group of people wanting to work together to realize a common vision.
- The number of individuals involved in the core group can be crucial.
- Too many people in the core group can certainly slow things down but can also result in a better constructed plan.
- There are different ways of contacting members:
  - ➔ word of mouth; by means of posters; handing out brochures or leaflets at public events; organizing a forum for a , Mass media (radio, press, television).

### **Step no.2: Carrying out a feasibility study**

carried out either:

- by a few members of the cooperative if they have the necessary skills and time, or
- by an outside person taken on by the cooperative.

The feasibility study is broken down into six parts:

1. An environmental study aimed at a better understanding of the socio-cultural scope of the cooperative;
  2. A market study
  3. A technical study : buildings, machinery, tools, etc. ;
  4. A study of the organizational structure
  5. A legal study .....legal format;
  6. A financial study .....the total expenses and products of the cooperative and its foreseen results.
- If the feasibility study proves inconclusive, the core group will have to steer itself towards another project.
  - If the study is conclusive, the group will pass on to the next step.

### **Step no.3: Drawing up a business plan**

- Plan is a planning tool to describe the future direction of a business.
- It is very useful for possible requests for loans or funding

- It helps to reveal the activities of the cooperative which will need more sustained effort.

The business plans:

- states the objectives ;
- identifies the monetary and human resources necessary ;
- describes how these resources will be obtained;
- explains why this enterprise will be successful.

#### **Step no.4: Organizing the inaugural general meeting**

- After working out the rules and internal administration of the cooperative, members must hold the inaugural general meeting,
- bringing together the entire membership of the cooperative.
- It is this meeting which is responsible for the adoption of the cooperative's rules and regulations/ by-laws as well as the business plan.
- It elects the members of the board /management committee.

#### 6.2. Registration of cooperatives

#### **Step no.5: Applying for registration and/or consent for the cooperatives**

- Registering the cooperative with the appropriate administrative authorities
- To explain, by obtaining moral person status for their cooperative, (limited liability)
- If the loan is not repaid, the personal property of members cannot be threatened,
- The date of registration corresponds to the date of official recognition of the cooperative.
- The request for registration must contain certain basic information about the cooperative:
  - The cooperative's trade name:
  - The cooperative's objectives
- Details of the cooperative's funding: shares .
- Internal administration of the cooperative
- The names of the cooperative's directors (management bodies) :
  - management committee, control committee, boards of director
- Some cooperatives may choose not to apply for registration and carry on their business illegally.
- Approval:
- A request for approval must usually be accompanied by the following items:
  - A copy of the rules by-laws of the cooperative;

- A certificate confirming the registration of the cooperative;
- The amount of share capital and its spread among the different members;
- Approval for the cooperative can be withdrawn if it is proved that it is not meeting the objectives for which it was set up.

### **Step no.6: Getting the cooperative started**

- At this stage of setting up the cooperative,
  - to select and recruit workers,
  - organize a programme of job training for them and
  - finally start up the cooperative's activities.

## **6.3 Organizational structure and financial organization of a cooperative**

### **6.3.1. Administrative Organizational structure**

- the decision of the members/ GA is final in all matters,
- The organization of a cooperative is inscribed in its rules/ by-law.

The different bodies

- There are two forms of organization,
  1. one made up of a Board of Directors and its chairperson, /Classical structure vs alternative structure
  2. The other consisting of a Management Committee and a Supervisory Committee.

The General Meeting/ Assembly

- The General Meeting is the sovereign body of the cooperative.
- It is the source of all authority and all power within the cooperative

Composition

- All members of the cooperative are part of it/GA and have an equal right to participate and be heard.
- Role of GA is described in the by-law
- The General Meeting cannot alone run the cooperative.
- It thThe Board of Directors
- The Board of Directors takes on the day-to-day running of the cooperative.
- Composition
- It is composed of a variable, but legally fixed, number of members elected by the General Meeting for a set period but usually eligible for re-election.

- The Auditor
- The auditor represents, for the entire membership of the cooperative, an aspect of financial control that is permanent and independent of the Board of Directors.
- Elected by the General Meeting, s/he presents a report and is answerable to it.
- The auditor has the right to convene it if s/he sees fit.
- His/her role is limited to monitoring rather than managing.
- It therefore generally delegates part of its authority to the Board of Directors.

#### The Board of Directors

- The Board of Directors takes on the day-to-day running of the cooperative.
- Composition
- It is composed of a variable, but legally fixed, number of members elected by the General Meeting for a set period but usually eligible for re-election.

#### The Auditor

- The auditor represents, for the entire membership of the cooperative, an aspect of financial control that is permanent and independent of the Board of Directors.
- Elected by the General Meeting, s/he presents a report and is answerable to it.
- The auditor has the right to convene it if s/he sees fit.
- His/her role is limited to monitoring rather than managing.



Figure 3: Diagram of the classical structure of a cooperative

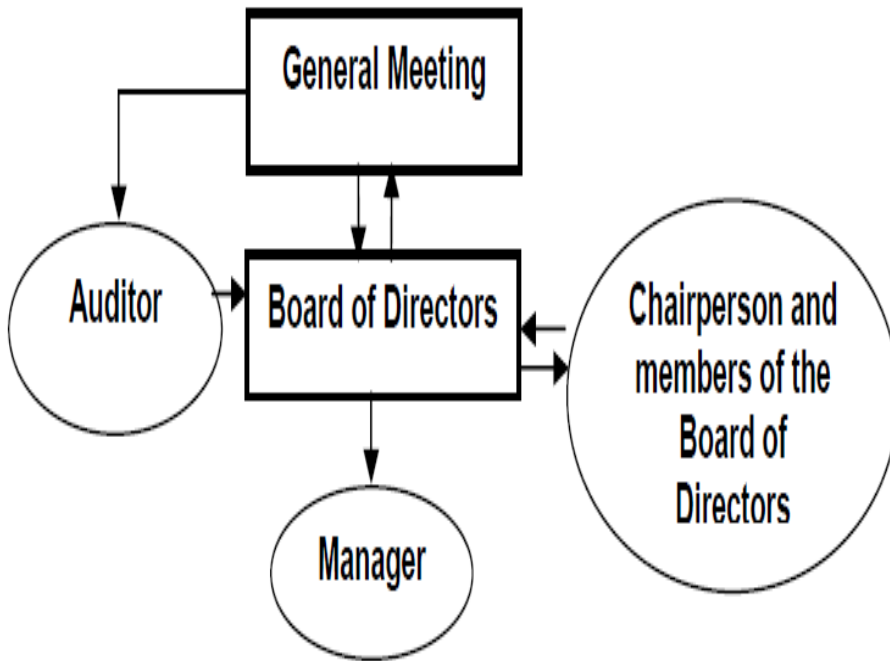
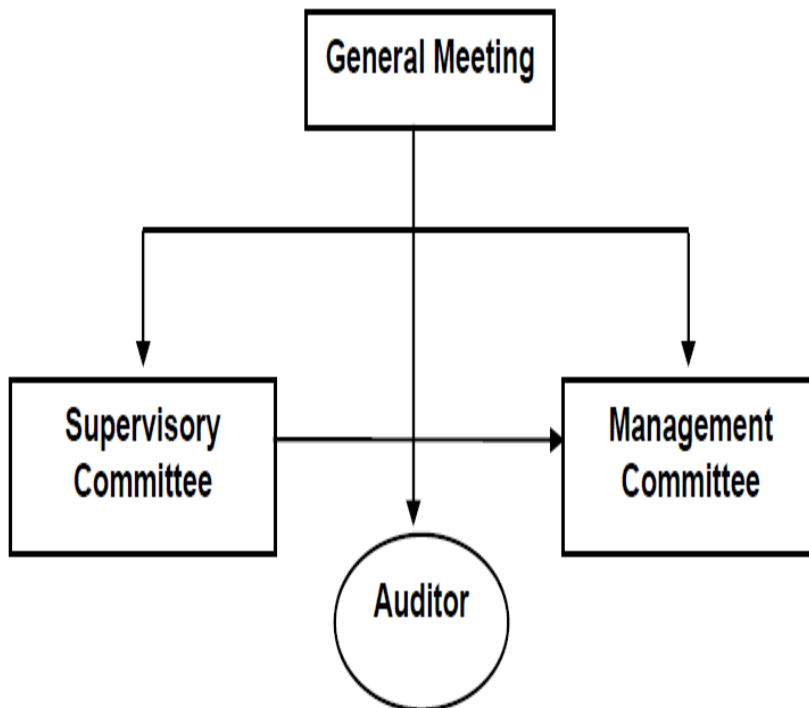


Figure 4: Diagram of the alternative structure of a cooperative



- The above figures are a diagram showing the classical structure of a cooperative and alternative structure
- These two types of organization rely
  - on the active and ongoing participation of members and
  - on the democratic nature of a cooperative.
  - The General Meeting has a considerable part to play, in the sense that it is the foundation and source of all the bodies that are linked to it.
- The principle of “one member, one vote” assumes that each member must be involved in the running of their cooperative;
- the successful running of the cooperative relies on its members

### **6.3.2. Financial structure**

- In the case of a cooperative, financial structure can take four forms:
  - a) Share subscription;
  - b) Borrowing;
  - c) Building up of reserves;
  - d) Donations and bequest /heritance, gifts.

#### **a) Share capital**

- The total shares subscribed by all members.
- The assets needed to make the cooperative work includes:
  - “fixed assets”, assets or property meant to be used on a long-term basis for running the cooperative’s operations.
  - working capital”. Other assets are destroyed the first time they are used for running the cooperative’s operations.
- Generally speaking, in developing and transitional countries, members of a cooperative have very little in the way of resources, sometimes not enough to contribute to shares.
- Then it is possible to substitute with payment in kind such as construction work, transportation of materials, secretarial work etc.
- It should be noted that you are qualify for membership as soon as shares are subscribed.

#### **b. Surpluses and reserves**

- The surpluses of a cooperative can be allocated in three different ways:
  1. To strengthen the capital base, by establishing reserves;

2. to pay a “dividend”;
  3. To pay members limited interest on capital.(in Ehio. Can’t be > banks interest rate)
  4. The reserves of a cooperative are collective and only in exceptional cases can they be distributed to members.
- This reserve fund allows the cooperative to mitigate the effects of periods of weak activity/ minimize risks.
  - In Ethiopia 30% reserve

### **3. Borrowing**

- A cooperative might have to borrow to make up for lack of capital.
- Considering the desire for independence and autonomy of cooperatives borrowing from within the membership is preferable.
- A large number of cooperatives, particularly consumer cooperatives, have acquired enough resources for little outlay by :
  - encouraging and collecting savings from their members in the form of interest-earning deposits payable on demand or at a due date.
- The other possible source of finance:
  - Credit Unions are one example.
  - Cooperatives which have proved their soundness can also issue bonds to their members or
  - encourage them to subscribe extra shares although such shares in no way change the rule of “one member, one vote”.
  - Finally, as a last resort, the cooperative can appeal to banks or other financial institutions.
- The personal property of members is not affected by the cooperative’s borrowings.
- It must take certain basic precautions such as making sure that there are enough funds immediately available to cover short-term debts.
- The goal here is not to make the greatest profit, but to give the best service to its members.

### **Horizontal and vertical structure**

#### **A. Horizontal structure /horizontal integration**

- It is the collaboration of cooperatives operating at the same level.
- This collaboration can be:
  - exploit the same plot of land as perhaps in the case of agricultural cooperatives;
  - Joint in the marketing or manufacturing of products.
  - in mergers of cooperatives: create a new cooperative to reduce costs, among other things.

### **B. Vertical structure:**

- It represents the hierarchical organization of the cooperative movement notably through :
  1. the Unions, it is a group of at least two cooperatives whose business purposes are identical or complementary.
  2. Federations : at least two Cooperative Unions can form a Federation
  3. Confederations of cooperatives (the cooperatives' cooperatives). It is called an apex organization of the cooperative movement.

Above all a Confederation acts in the following ways:

- it takes on the role of spokesperson at the national level of government and related authorities for all questions relating to the cooperative movement;
- it prepares and circulates statistical data about the cooperative movement;
- it advises on the general direction of national cooperative policy
- It represents the cooperative movement at regional, national and international level.

## **6.4. Management of cooperatives**

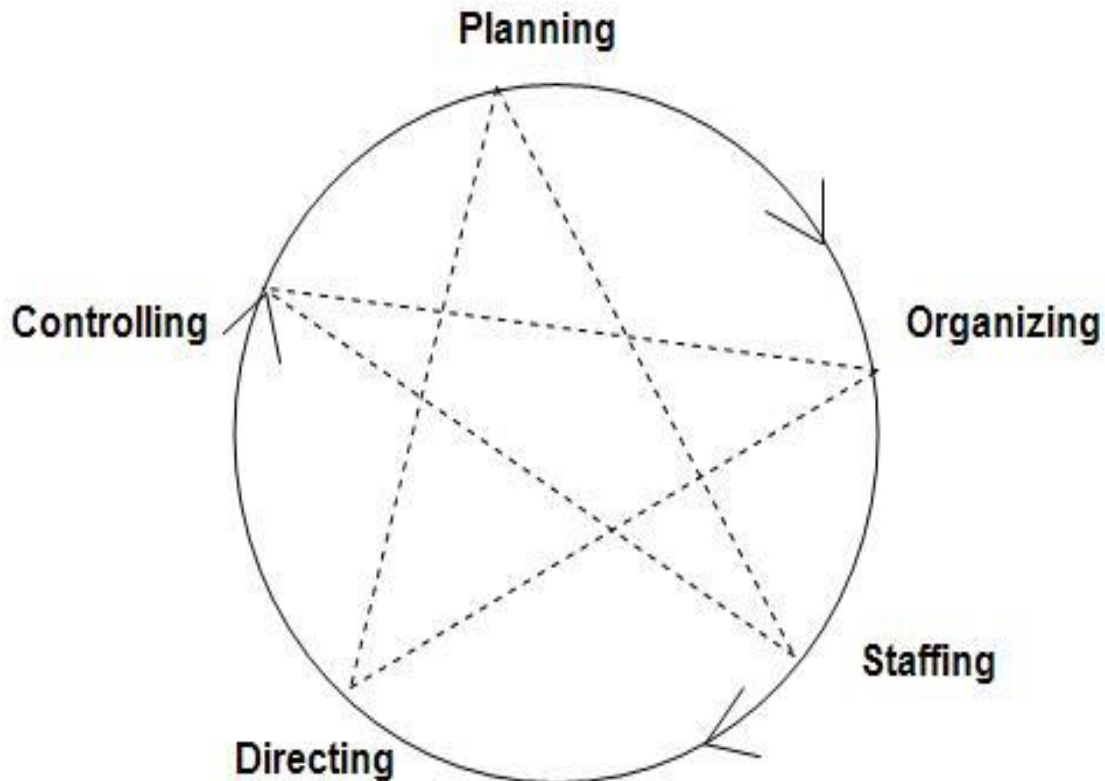
### **6.4.1. Management concept**

- Getting things done through others.
- Process of directing resources in an efficient and effective manner toward the accomplishment of organizational goals.
- It is a dynamic process consisting of various functions.

### **6.4.2. Functions of Management (FoM)**

- Different experts have classified functions of management in different ways. Luther Gullick has given a keyword 'POSDCORB'
- But the most widely accepted given by KOONTZ and O'DONNELL  
i.e. Planning, Organizing, Staffing, Directing and Controlling.

- these functions are overlapping in nature i.e. they are highly inseparable.



### 1. planning

- It is the basic FoM.
- It deals with a future course of action & deciding in advance the most appropriate course of actions for achievement of pre-determined goals.
- is deciding in advance - what to do, when to do & how to do. It bridges the gap from where we are & where we want to be”.
- is a systematic thinking about ways & means for accomplishment of pre-determined goals.
- it also helps in avoiding confusion, uncertainties, risks, wastages etc.

### 2. Organizing

- It is the process of bringing together physical, financial and human resources and developing productive relationship amongst.
- determining & providing human and non-human resources to the organizational structure.

- As a process it involves:
  - Identification of activities.
  - Classification of grouping of activities.
  - Assignment of duties.
  - Delegation of authority and creation of responsibility.
  - Coordinating authority and responsibility relationships.

### **3. Staffing**

- Manning the organization
- It is to put right man on right job i.e. square pegs in square holes and round pegs in round holes.
- Staffing involves:
  - Manpower Planning (estimating man power in terms of searching, choose the person and giving the right place).
  - Recruitment, Selection & Placement.
  - Training & Development.
  - Remuneration.
  - Performance Appraisal
  - Promotions & Transfer.

### **4. Directing**

- It actuates the organizational methods to work efficiently
- It is influencing, guiding, supervising, motivating sub-ordinate for the achievement of organizational goals.

It has the following elements:

1. Supervision- overseeing the work of subordinates by their superiors. It is the act of watching & directing work & workers.
2. Motivation- means inspiring, stimulating or encouraging the sub-ordinates with zeal to work. Positive, negative, monetary, non-monetary incentives may be used for this purpose.
3. Leadership- may be defined as a process by which manager guides and influences the work of subordinates in desired direction.

4. Communications- is the process of passing information, experience, opinion etc from one person to another.

It is a bridge of understanding.

### **5. Controlling**

- measurement of accomplishment against the standards and correction of deviation if any to ensure achievement of organizational goals.
- It is the process of checking whether or not proper progress is being made
- Controlling has following steps:
  - Establishment of standard performance.
  - Measurement of actual performance.
  - Comparison of actual performance with the standards and finding out deviation if any.
  - Corrective action.

## Chapter 7. Forms of Business Organization

Chapter objective:

☞ At the end of this chapter students should able to:

- ❖ Describe forms of **Business organization** and their similarities and differences
- ❖ Explain the criteria for choosing legal form of business **organization**

Various legal forms of business organizations are available to organize businesses. These include: Proprietorship, Partnership, Corporations, and Cooperatives. Each form of ownership has a characteristic internal structure, legal status, size and field to which it is best suited. Each has key advantages and disadvantages and offers employees a distinctive working environment.

### 7.1. The Sole Proprietorships

A sole proprietorship is a business owned by just one person, although it may have many employees. It is the easiest form of business to start with limited funds. This person, also called a proprietor, is classified as self-employed. Sole proprietorship is the most common form of ownership among small businesses and can be cited as the first stage in the evolution of the forms of business organizations. The owner furnishes money, management, and perhaps part of the labor; moreover, the owner is entitled to all profits earned by the business but also assumes the risks in which the business is exposed.

#### Advantages of Sole Proprietorships

*Ease and low cost of formation and dissolution:* The first and most concrete advantage is that, it is relatively easy to establish. The financial investment need not be large, and legal red tape is minimal. It is simple to establish because there may not be a need for making it formal. Even if it is to be formal there may not be a need to pass through detailed bureaucratic procedures.

*Owner-ship of all profits and personal incentive:* There is complete ownership of all profits. All the profits belong to the proprietor. They do not have to be shared with anyone else. It is he who faces the loss and this gives great incentive to the owner to take personal care and manage it efficiently.



*Freedom and promptness of action:* Another advantage is the concentration of authority that simplifies running the business. The sole proprietor is not blocked in making decisions; he can take his own decision because he has full authority over his firm. The sole proprietor can take prompt decisions especially when an emergency arises.

*Business secrecy:* It is easy to maintain the secrecy, of the business since confidential information is one of the factors, which bring success, then it is much more safe here than other type of businesses. The owner never has to reveal his performance, plans or intentions to anyone else.

*Social desirability:* From the social point of view, the sole proprietorship is desirable as it ensures that too much wealth doesn't concentrate in a few hands. It may be one of the ways in which equitable distribution of wealth is ensured.

*Pride of ownership:* People who own and manage their own businesses are rightfully proud of their work. They deserve all the credit for taking the risks and providing needed goods or services.

*Single tax (tax breaks):* A major advantage of the proprietorship is that the business pays no income tax. All the profits of a sole proprietorship are taxes as the personal income of the owner, and he/she pays the normal income tax on that money.

### **Disadvantages of Sole proprietorships**

*Unlimited liability-the risk of losses:* The sole proprietor will be legally liable for all debts of the business. At times of loss and bankruptcy if the business asset is not sufficient to satisfy the obligation or settle debts of creditors, his personal and real property may be required to pay off.

*Limited financial resources:* Funds available to the business are limited to the funds that the one (sole) owner can gather. A sonly one person is responsible for the business, the capital is limited to his capacity particularly o operate a large-scale business enterprise.

*Limitations in managerial ability & other special skills and abilities:* While running a business, many complex and difficult problems may arise, requiring wide array of knowledge in management. Operating a business requires planning, organizing, controlling, marketing, financial, motivational, and customer relations' skills. Rarely does an individual have this range of needed expertise.

*Uncertain future:* This kind of business suffers from uncertain future, which means there is lack of stability or lack of continuity. Death, illness, bankruptcy, or retirement of the owner terminates the proprietorship.

*Demands on time (overwhelming time commitment):* It is hard to own business, manage it, train people, and have time for anything else in life. The owner must spend long hours working to develop a customer base, especially when the businesses new.

*Difficulty in hiring and keeping high achievement employees:* A good employee of the business may quit because there is no opportunity to obtain an ownership interest in it.

*Few fringe benefits:* If you are your own boss, you lose many of fringe benefits that come from working for others.

## **7.2. The Partnership Option**

A partnership is a business run by two or more persons where their relationship is based on agreement participating in the profits and losses arising out of it. Or it is an association of two or more persons to carry on as co-owners of a business for profit. Partnerships are voluntary associations, and most are relatively small businesses. They are the least popular forms of business ownership.

### **Characteristics of Partnership**

*Formation:* This form of business requires the existence of two or more persons entering in to contractual relationships. The agreement between parties is desirable to be written and signed, to prevent misunderstanding among the parties. This contract is called memorandum of association, articles of partnership deed or partnership contract. Partner's rights and duties should be explicitly in written articles of partnership.

*Capital contribution:* Every partner shall make a contribution, which may be in at the form of money, receivables, property or skill. The contribution to be made for the business shall be equal unless otherwise agreed.

*Management:* If there is no agreement as to the pattern of managing the business, every partner has the right to take active part in the management of the business affairs. Partners can make an agreement how to share the responsibility among themselves according to their experience and knowledge.

*Duration:* Legally a partnership comes to an end or terminated for various reasons. It is terminated when any of the general partners withdraws dies or become no longer to be a partner. However, if there managing partners agree to continue under the original name of the firm and style, they can continue after settling the claims of the outgoing partner. The partnership can be dissolved prior to the expiry of term when they agree to terminate.

*Other legal characters:* As in sole proprietorship, in a partnership each partner is personally liable for the obligations of the business. Furthermore, if one partner's decision costs the company money, it affects all the other partners, who may have to pay for losses out of their personal assets.

### **Advantages of partnership**

*Ease of starting:* Because it involves a private contractual arrangement, a partnership is fairly easy to start. It is nearly as free from government regulations as a sole proprietorship. The cost of starting a partnership is low; it usually involves only modest legal fee for drawing up a written agreement, which is highly desirable. An oral agreement is sufficient but not recommended.

*Increased sources of capital and credit:* The partnership offers numerous sources of capital. First, there are the direct contributions from the partners themselves. Second, there are the loans that friends, investors, and lending institutions are willing to make. Third, there is the credit that suppliers will extend.

*Combined managerial skills (improved decision making potential):* A partnership is likely to be operated more efficiently than a proprietorship because two or more persons share in the management and there is a good chance that a partnership will make better decisions. This is particularly true if the partners are specialists in different areas. As a result there can be a host of partners who each contribute to a particular specialized area. Thus overall decisions are improved, which provide a greater chance of success.

*Definite legal status:* Partnerships have been in existence for centuries. The questions of rights, responsibilities, liabilities, and partner duties have been covered. Thus the legal status of the partnership is clearly understood.

*Personal supervision:* Partners look after the business personally and guard against wastage and other insufficiencies because they are initially interested in the success of the business, and also know if there is any failure on their part, they may put even their private property in jeopardy.

*Reduced risk:* The losses incurred by the firm will be shared by all partners and hence the share of loss of each partner will be less than in case of sole proprietorship.

*Motivation of important employees:* There is an incentive for employees to make a personal contribution to the business if the possibility exists that they may become partners in the business.

*Tax advantages:* The partnership has some potential tax advantages over a corporation. In a partnership, as in a sole proprietorship, the owners pay taxes on the business earnings.

### **Disadvantages of Partnership**

*Unlimited liability:* Although this point will make the partners not to be careless, it might make partners fear of taking advantages of sudden business opportunities.

*Risk of implied authority:* Each partner is bound by the partnership contracts made by any partner if such contracts apply to the ordinary operations of the business.

*Lack of harmony:* Decision made by several peoples (partners) are often better than those made by one. However, having two or more people deciding on some aspect of the business can be dangerous. Power and authority are divided and the partners will not always agree with each other. As a result poor decisions may be made. Also, decision-making becomes more time consuming because agreement must be reached before action can be taken.

*Lack of continuity (instability):* If any one of the general partners dies withdraws or becomes mentally or physically incapacitated (injured), the partnership ends.

*Limited capital availability (size limitations):* There is a limit to the capital and credit that bankers and suppliers are willing to provide. Therefore, sooner or later, the firm will find its growth limited.

*Investment withdrawal difficulty (frozen investment):* A person who invests money in a partnership may have a hard time withdrawing the investment. The money typically considered a “frozen-investment” is tied up in the operation of the business.

### **7.3.The Corporation Option**

The corporations have emerged and grown up to overcome the above-mentioned shortcomings of the previous forms of organizations and meet the increased need of modern and large scale of industry and commerce. Corporations are towers on the business landscape. While

proprietorships are many in number, they are generally small in size. In comparison, corporations are few in number, but generally large in size. Because corporations tend to be large, they play a powerful role in the economy of our country. The most widely quoted definition for joint stock company or corporation is given as an artificial person (being an association of natural persons) authorized and recognized by law, with distinctive name, a common seal, comprising of transferable shares of fixed values, carrying limited liability and having a perpetual or continued or uninterrupted succession life.

### **Characteristics of Corporation**

*Separate legal entity*-The definition of corporation given above begins by asserting that a company is an artificial person. This indicates that, on the one hand it is not a natural person or physical person like a human being. On the other hand though it is not a natural person, having existence in the eyes of law and considered as an artificial person created by law, have many of the rights of the natural person. All the rights, duties, status of a corporation stem from the charter of the country. To get a permission to form a corporation, a charter is needed. A charter is a document issued by the country authorizing the formation of corporations. A charter is the official document giving power to run a corporation. It is often called a certificate of incorporation. A Corporation is a legal entity separate from the natural persons connected with it. Therefore, the shareholders cannot be held liable for the acts of the corporation. Shareholders being natural person (entity) distinct from that of the company can sue the company and be sued by it.

*Limited liability*-Since the corporation has separate legal entity its debts are its own. The assets and liabilities, rights and obligations incidental to the company's activities are assets and liabilities, rights and obligations respectively of the company and not of its members. Their personal assets cannot be seized to pay the debts of the corporation.

*Transferability of shares*: It is easy to transfer ownership in a corporation. A stockholder may sell stock to another person and transfer the membership and membership interest freely without consulting other stockholders.

*Death and Withdrawal of shareholders*-Unlike the partnership, ownership in a corporation is readily transferable. Exchange of shares of stock is all that is required to convey an ownership

interest to a different individual. In a large corporation, stock is being exchanged constantly without noticeable effect upon the operations of business. The death of the majority stockholders could be equal unfortunate. To prevent problems of this nature from arising, legal arrangements should be made at the time of incorporation to provide for management continuity by surviving stockholders, as well as for fair treatment of heirs of a stockholder.

*Common seal*-A corporation has a common seal with the name of the company engraved on it, which is used as a substitute for its signature though it acts through its agents. A company cannot sign documents for itself-being an artificial person.

*Separations of ownership from management*-All shareholders (owners), large in number, do not have the opportunity of managing the day-to-day activity of the corporation. The stockholders who own the capitals are kind of absent owners who are engaged in their respective other personal work while holding shares of the company. The company is free to hire any employee it can afford and is thus able to get the specialized professional skills needed for sound management.

*Supervision*- A Company is created by the legal process of incorporation. It exists as an artificial person until it is formally dissolved by removal of its name from the register at the company registry. While it exists it is subject to detailed regulation; for instance, it must prepare and deliver to the registry annual accounts and an annual return (a summary of its situation).

*Written constitution*-A company has no mind of its own to decide what to do. The structure of divided control between directors and members must be clearly defined. A company therefore has a written constitution. On the creation of a company, the promoters must file certain documents with the Registrar of Companies. These include the Articles of Association and the Memorandum of Association. The articles contain details of how the company will be run from day to day. The memorandum lays down the constitution of the company.

*The Corporate Charter*- In most states, three or more persons are required to apply to the secretary of state for permission to incorporate. After preliminary steps, including required publicity and payment of the incorporation fee and initial franchise tax, the written application is approved by the secretary of the state and becomes the corporation's charter.

Advantage of a corporation

*Financial strength*-No other forms of business ownership can match the success of the corporation in bringing together money, resources, and talent, in accumulating assets, and increasing wealth.

*Limited liability*-The owners (stockholders) are not legally liable for the debts of the corporation beyond their investment in the corporation. Because the corporation is a legal entity, it is responsible for its own debts, but not its stockholders. Thus, it can attract more investors who do not want to take risk.

*Scopes of expansion*-Corporations have greater growth potential than sole proprietorship or partnerships because they can raise more capital by selling stocks and bonds.

*Managerial efficiency*-Corporations enjoy the advantage of efficient management by hiring specialists or skilled persons to become members of the board of directors to manage the corporation. If corporations found managers to be unsatisfactory they can be fired and replacing them with outstanding ones.

*Ease in transferring ownership*-In almost all instances stockholders can sell their shares to anyone willing to buy them. In the case of death, the shares of deceased stockholders can be transferred to their heirs.

*Legal-entity status*-A Corporation can purchase property, make contracts, sue and be sued in its corporate name.

### **Disadvantages of a Corporation**

*Difficulty of formation*-It is time consuming and cumbersome to establish corporations' unlike the other forms of businesses. Corporations require large sum of money, which a large number of people have to be approached for raising this capital. Moreover, there are some restrictions by the state charter.

*Lacks of owner's personal interest*-These forms of organizations are managed by directors and hired officials and employees who may not be expected to have such an interest in the success of the business as the individual owner or partner would have in his own business.

*Delay in decision making*-An incorporated organization usually does not enjoy the same amount of flexibility and promptness of decisions as a sole proprietorship organization. Decisions especially on key issues requiring general meeting of shareholders may be delayed because of the time interval between meetings, difficulty of getting the required number of members to pass

decision or the requisite quorum, and the presence of diverse interests which may lead to disagreements.

*Oligarchy and fraudulent management*-Although in theory it is said democratic principles are followed in the management of the companies, in practice the concentration of managing power is in the few hands of managing directors, thus, leading to oligarchy of managing or rule by few. Many times dishonest persons at the top succeed in clearly misleading and cheating the shareholders and as a result leading the companies to be managed by cheating and fraudulent hands.

*Lack of secrecy*: Large companies suffer from lack of secrecy in their financial affairs. Corporations are required to make annual reports to government agencies as well as to their shareholders. Thus, financial details become available to competitors, as well as to the general public.

*Double taxation*: Corporations, with the exception of S-corporations, are subject to double taxation: first the corporation pays taxes on its profits and then after it distributed some of these profits to shareholders, the shareholders pay taxes on the dividends (income) they receive.

*Relative lack of credit*: Sizes for size, corporations do not enjoy the credit standing of proprietorships and partnerships because of the limited liability of their stockholders. Banks and other lenders have to consider the limited liability of corporations. If corporation fails; its creditors can look only to the assets of the business to satisfy claims.

#### **7.4. Cooperatives**

A Cooperative is a business owned and operated by its user-members for the purpose of supplying themselves with goods and services it is an organization owned by members/customers who pay an annual membership fee and share in any profits (if it is profit making organization). Owners, managers, workers, and customers are all the same people. These cooperatives are formed to give members more economic power as a group than they would have as individuals. It can register and have limited liability for its members, but has to adopt the following principles: members have an equal vote in decisions; membership is open to everyone who fulfills specified conditions assets controlled, and usually owned jointly by members; profit shared equally between members with limited interest payable on loans made by members; share capital remains at its original value-members benefit from participation, not investment.



### Criteria for choosing legal form of business ownership

A number of criteria must be considered and some tradeoffs are necessary. These are:

1. Organizational costs
2. Limited versus unlimited liability
3. Continuity
4. Transferability of ownership
5. Control
6. Raising new equity capital
7. Income taxes

**Below is the summarized brief of types of business organizations.**

<b>Organizational characteristics</b>	<b>Individual proprietorship</b>	<b>Partnership</b>	<b>Corporation</b>	<b>Cooperative</b>
Ownership	Single individual	Partners	Share holders	Member Patrons
Management control	The proprietor	The partners	Board of directors	Board of directors
Management orientation	The proprietor	The partners	Share holders	User members
Objectives	Profit for the proprietor	Profit for the partners	Profit for the stockholders	Service for the member patrons
Primary Users	The public	The public	The public	Member patrons
Ownership representation	The proprietor	Based on Legal agreement of partners law	The investors One vote per share owned	Members based on one man one vote principle
Legal base	Unincorporated	Legal agreement of associates under law	Incorporated under law	Usually incorporate under special enabling legislation
Liability	Unlimited	Unlimited	Limited	Unlimited
Proceeds recipients	The proprietor	The partner	The share holders	Members - Proportionate to

			proportionate to number of share holdings	patronage
Return on invested capital	Unlimited	Unlimited	Unlimited	Limited by law

### Learning Activity

1. Explain the main characteristics of the following forms of business organization:
    - ✓ Sole proprietorship
    - ✓ Partnership
    - ✓ Corporation
  2. Discuss on the advantages and disadvantages of the above mentioned types of business organizations.
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3. What are the salient features that distinguish cooperatives from other business organizations?
  4. What are the distinguishing features of sole proprietorship and partnership types of businesses?
  5. What are the unique characteristics of cooperatives?

### Major References

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