

Demutualization of Cooperatives: Reasons and Perspectives.

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Abstract

This study will attempt to find out why cooperatives are demutualized. The article tries to define what is this process of demutualization in cooperatives. It shows cases of demutualization of cooperatives in various part of the world in order to find out common denominators for this process of demutualization of cooperatives.

The summary shows the various types of demutualization of cooperatives. It shows as well the various factors for demutualizations and divides them between internal factors and to external factors. It shows graphical models of these factors.

Interesting conclusions may be derived out of this trend of demutualizations, and which call to a redefinition of the ownership relationship between the member and the cooperative, and the ways members are rewarded for the participation in the cooperative. These two changes are the main points utilized by those who are against any change in the current 3rd ICA principle of member economic participation.

Introduction

The process of demutualization of cooperatives, sometimes called conversion, through which cooperatives turned to be private or public owned companies, is the subject of this study.

The discussion of the issue will start with the notions of demutualization and with its existing definitions in the literature on the subject. Later on, the discussion will analyze the causes and processes of demutualization, and trying to verifying their necessity, if existed. It will also examine demutualization processes in various part of the world, including Australia and New Zealand, the South East Asia, the European Union countries, North America and Israel.

The study will suggest similarities and differences in the process of demutualization various cooperatives worldwide experienced.

What is the demutualization process.

We find some definitions describing this process through which cooperatives cease to exist and become different economic structures and entities. This process is defined by Fabio Chaddad (Chaddad, 2003) (p.1) as:

"Conversion, increasingly known as demutualization, refers to changes in the ownership structure of user owned and controlled organisations from a cooperative (or mutual) to a for-profit, proprietary organisation."

The author wants to describe a situation of a cooperative structure where members are the owners of the structure-organization, and benefit from the fruits generated of their

active participation in the economic activities: this organization changes into a different one where the new owners benefit from the economic fruits based on the amount of ownership shares they hold. Members participation is replaced by capital participation.

This definition does not touch a central issue in cooperatives, which we shall discuss in details later: The central reason for conversion¹ of cooperatives is that members cease to get the service or the product at the price and quality they have been used to getting from their cooperative, and which was the reason that they established it or joined the cooperative.

David Griffiths defines (Griffiths, 2004) (p. 17) the process as a situation where:

"Demutualisation refers to the decreased use of mutual organizations to provide services and produce goods and the conversion from mutual to investor ownership. The beginning of demutualisation of a co-operative is when the co-operative has lost its cooperative identity and what distinguishes it from investor-owned companies."

In this definition a new element has been added, the cooperative identity, which is what makes the difference between cooperatives and other economic enterprises.

The Canadian cooperative Desjardins presents another definition of demutualization in a report on the subject. It adds further elements to the process. The President Director General of this giant financial cooperative Ghislain Paradis (Paradis,

1. Demutualization is synonym for conversion in our discussion.

2000) describes the process (p. 1) as:

"La démutualisation est ce processus qui conduit l'institution coopérative à troquer ses caractéristiques fondamentales, donc à perdre son identité, en vue d'obtenir des gains jugés préférables."

This definition brings the argument that the conversion process of cooperatives is mainly because in a non-cooperative economic structure the distributed benefits would increase.

Race Mathews gave another definition to demutualization. Mathews (Mathews, 2003) defines the process in this way(p. 7):

"Demutualisation – the conversion of member-owned mutualist²

2. In many publications about cooperative demutualization the words cooperative and mutual are almost synonymous.

Still, there are countries where mutual has another meaning. In France the term mutual refers to an organization which fulfills the role of an health insurance cooperative.

This site gives us an explanation of a mutual:

<http://en.wikipedia.org/wiki/Mutual>

A **mutual, mutual organization, or mutual society** is an organization (which is often, but not always, a company or business) based on the principle of mutuality. Unlike a true cooperative, members usually do not contribute to the capital of the company by direct investment, but derive their right to profits and votes through their customer relationship. A mutual organization or society is often simply referred to as *a mutual*.

A mutual exists with the purpose of raising funds (or money), from its membership or customers (collectively called its *members*), which can then be used to provide common services to all members of the organization or society. A mutual is therefore owned by, and run for the benefit of, its members – it has no external shareholders to pay in the form of dividends, and as such does not usually seek to maximize and make large profits or capital gains. Mutuals exist for the members to benefit from the services they provide.

Profits made will usually be re-invested in the mutual for the benefit of the members, although some profit may also be necessary in the case of mutuals to

bodies such as mutual assurance and insurance societies, friendly societies, credit unions and co-operatives into shareholder-owned proprietary limited companies".

In this definition we find an emphasis toward the financial co-operatives. The end product of the process is a different economic structure - the private shareholders limited companies. He mentions these cooperatives as those who inclined to be easily demutualized. It is interesting to note that all these co-operatives are characterized by the fact that their members are also their users in contrast to cooperatives where users are not members. It is too early to know if cooperatives whose members are not the users are not inclined to be demutualized.³

Factors causing demutualization

The demutualization process has raised the interest of scholars from the beginning of the 1980s, when many cooperatives and from different cooperatives branches have gone through this process towards becoming private companies. Chaddad (Chaddad, 2003) formulates some conclusions about this process. He found that waves of demutualization happened after the market has gone through structural adjustment with the various institutions inside it. Deregulation of markets, technological innovations or agro-industrial innovations, which change the "rules of the game". These changes increase

sustain or grow the organization, and to make sure it remains safe and secure.

For the French Mutuel see:

<http://www.mutuel.org/>

3. On the difference between cooperatives whose members are users and those whose members are not users see my article on producers cooperatives. (Galor, 2000)

competitiveness in the market, and this encourages demutualization of cooperatives.

More factors contributing demutualization were detected by Nadeau and Nilsestuen (Nadeau, E.G. and Nilsestuen, R, 2004) as detailed here:

- Seldom is demutualization an outcome of pressure made by the members themselves. In most of the cases demutualization derives out of pressure coming from the senior staff of the cooperative, from the members of the management board, by external advisers, most of whom may benefit from demutualization.

These two scholars, found other factors pushing forward towards demutualization:

- Cooperatives which neglected the cooperative education of their members, as well as those which decreased transparency of the cooperative affairs from members, have eased the demutualization process. To this, one can add the practice of low quorum needed by the cooperative when taking democratic decisions, and the ability to vote via proxy.

- The financial aspects also contributed: Difficulties in liquidity, financial problems, and financial incentives all increased pressure on management boards towards demutualization.

Chaddad (Chaddad, 2003) found that conversion of cooperatives into stock traded company increases the efficiency of the business and remove financial limitations for the new company. On the other hand, Nadeau and Nilsestuen (Nadeau,

E.G. and Nilsestuen, R, 2004) argue that in cooperatives which demutualized, members benefited on the short term, but in reality, they lost the control of their former cooperative. It can be summed up that findings show that members gained nothing out of the demutualization.

A very important factor, emphasized in some of the research by Sonja Novkovic (Novkovic, 2005) and in Yair Levi (Levi, 2000) is that there exists a difference in understanding of the cooperative and its enterprise among cooperative managers and among members of board of directors of cooperatives. It is clear that leaders of cooperatives at the higher levels lack the recognition, the knowledge and the understanding of what is a cooperative and what are the cooperative principles. We shall see, in latter phase of this study, that this was the case of the public transport cooperative in Tel Aviv.

In a recent study Alan Robb (Robb, 2006a) shows that the conversion of cooperatives in Australia was accelerated when appropriate laws which facilitated demutualization were enacted, which were backed by the usual justification, and which are known in other countries as: The conversion will increase accessibility of cooperatives to external capital; it will enlarge and expand the new created enterprise; it will enable to compete efficiently with other companies in the same sector.

This source mentions that in other research done in Australia in 1998 findings show that 23 years of comparison the business results of private companies and of cooperatives, showed that cooperatives were more efficient.

One of the arguments in favor of demutualization is that the market economy is minimizing the difference between the cooperative enterprise and Investment Led Firms (ILF). The arguments in favor are brought by Julie Hogeland (Hogeland, 2006) even though she is not supporting them. The private firm includes components and advantages as follows:

- The private firm has an advantage by the fact that it focused on one goal; to look for profit.
- The private firm has a broader view of the market than that of the cooperative. In looking, for example, for raw materials needed by the private firm, the view is global to where the cheapest raw materials can be found.
- Constant growth, increased efficiency, and better sources of external capital bring better survivability and expansion.

Contrary to the private firm, the cooperative has the following advantages since it advances various values:

- Defending the members of the cooperative and their employment. The cooperative provides a secure employment environment to its members.
- In rural areas, the cooperative contributes to enhancement of the rural community.
- The fact that the members own their cooperative ensures their control and inspection over the future of their cooperative.

Even though the conversion processes of cooperatives into

private companies exists, still it is not so frequent. Nevertheless, this conversion situation needs preventive and defending measures by the cooperatives. These preventive measures include changes in the cooperatives' bylaws, steps towards bringing members nearer to their cooperatives and to their communities, and even changing the cooperative law. Nadeau and Nilsestuen (Nadeau, 2004) continue and showing that in cooperatives where the level of participation in cooperative democratic life was high - such as cooperatives which integrate members in its various activities, and which are linked vividly to the community - were more resistant to the aggressive pressures to demutualize.

The study shows that consumer cooperatives and electricity supply cooperatives are more vulnerable to demutualization. Insurance cooperatives were more exposed to demutualization than the ones mentioned above. It was also found as well that in the middle of the 1980s half of the insurance market in the USA was held by the insurance cooperatives. But in 2001 the insurance cooperatives accounted for only 17% of this market. The study found that in these cooperatives the level of member involvement was very low, and that most members of these cooperatives understood almost nothing about what is a cooperative, and their identity as the owners of the business.

Further findings of this study show that in cooperatives for the supply of electricity and communication services there was only one case of demutualization since 1940. The factors against demutualization in these cooperatives are:

- The statutes of these cooperatives or the state bylaws determine that these sorts of decisions could be passed only in

general meetings where the quorum level is very high.

- In these cooperatives, member involvement is very high. It was found that the members are aware and they are updated, about what is going on in their cooperatives, and are satisfied from the services supplied to them by the cooperative.

- These cooperatives are supported by cooperative federations to which they are affiliated or by apex organizations, and these bodies actively support their member cooperatives when under demutualization pressures.

And indeed, Paul Hazen, who is President of the US apex organization (Hazen, 2004) confirms that members who are better served by their cooperatives, and who feel that their voice is heard and influences cooperative policy, are highly loyal to their cooperative. Member involvement in the cooperative life in all its aspects increases the chance that demutualization would be a very difficult process in such a cooperative.

Johnston Birchall (Birchall, 2002) also determines that when cooperative management and their directors encourage members to actively participate in the cooperative activities, the chances of having success is higher than in other organizational structures.

David Griffiths (Griffiths, 2007) thinks that the internal factors in the cooperative are more important than the external ones when considering demutualization. The reasons are related to the presence of the following:

- Employed managers and members of board of directors who seek the immediate gain in the cooperative as a short term goal, and who are not concerned about any commitment to the cooperative values and principles.
- Members of board of directors who become prisoners of the employed managers of the cooperative and who forgot that their role is to protect the cooperative identity. The cooperative identity and the cooperative principles are wrongly regarded by many, as only historically important, and not relevant to today's economic life.
- External advisers employed by board of directors who are engaged by management to help in formulating future management decisions, but are ignorant and hostile to the cooperative values and principles. While they are external players, the decision to employ these advisers is an internal decision of the cooperative.
- Members whose membership is idle, as old and veteran members, and who are practically disconnected from their cooperative, and at the same time failure of management to advance the values and the identity of the cooperative among members.
- The lack of ongoing cooperative education to the management, to members of board of directors, to employees of the cooperative, and to the members of the cooperative. Cooperative education is vital to the existence and to the development of ownership and control of members on their cooperatives.

Garry Cronan (Cronan, 1994) identifies four groups of factors

which ease the movement toward demutualization. He refers to Australia, but as we shall see later in this study, his observations are valid for other countries as well:

Structural factors are most important. Among them he identifies the property and capital components in the cooperative. Lack of capital in the cooperative is a major factor leading to demutualization. Many of the cooperatives are utilizing, when in need, members' capital and undivided reserve funds. The fact is that members' shares are almost without financial value, and their returns are limited by the 3rd ICA cooperative principle, limits the cooperative ability to mobilize needed finance. There is an understanding that the demutualization process "frees" the hidden value of members' shares, especially for those members who are no longer active in the cooperative.

Cronan finds further structural factors, helping to demutualization, in the fact that there is a shortage or absence of representative cooperative federations and apex cooperatives, the fact that there is no cooperation among cooperatives, and that the cooperative culture is neglected or nonexistent. All these, contribute to demutualization.

Additional factors are the low level of management skills specific to cooperatives, and the lack of understanding among management of what is a cooperative. The lack of supporting policy from government for the cooperative cause adds to previous reasons mentioned above.

In 2006 a parliamentary commission in England published a report written by Ian Welch (Welch, 2006) . The commission

examined whether cooperatives which went through demutualization have improved their financial performances compared to cooperatives which remained as such. The same questions were asked referring to the quality of services rendered by them.

The report finds that cooperatives which did not go through demutualization have shown better performances than those which went demutualization. At the same time the report shows that directors of cooperatives which were demutualized have benefited from considerable financial rewards, but did not show improved performances. The commission found much evidence that members of cooperatives who vote for demutualization did not fully understand what they were voting for. Further evidences show that after demutualization, members have been charged with expenses which swallowed almost all benefits to which they were entitled for.

This view is shared by the council for enterprises, employers and social economy groups, (CEGES, 1997) (CEGES) Conseil des Entreprises, Employeurs, et Groupement de l'Economie Sociale) which reports that the evidence gathered in France shows that financial cooperatives, which have not demutualized, served their members at a lower cost than those which did.

Another problem observed among members of board of directors⁴ is their lack of knowledge and their lack of abilities to

4. Board of directors is a synonym to the term Management Committee. Both terms are utilized in various countries.

ask the appropriate questions to the managers of the cooperatives and to employees of the cooperatives, when they came to recommend demutualization. A study by Cornell University (Anderson, & Henehan, 2002) found that members of boards of directors of cooperatives should receive the appropriate answers from the managers and employees of the cooperative before any decision towards demutualization.

One of the issues to which cooperatives facing pressure to demutualize should consider is the issue of raising supplementary financing when the cooperative is in need. Viewing this issue Beth Baker (BAKER, 2002) raised the question of whether the cooperative is able to compete efficiently, and should be able to mobilize supplementary financial resources in the financial market. Further questions were asked:

Is this is a search after supplementary finance for the cooperative or these are steps done by the management committee or by the directors, and sometime by the will of members, to translate the success of the cooperative into cash money.

Apparently, the more the cooperative succeeds, the lower the attention members paid to the way the cooperative is run, and higher their reliance on their management team.

The research mentions the case of IGA Federal Credit Union of Feasterville Pennsylvania. In 1998, ten management members led the first conversion of a credit union in the USA, into the format of a Mutual Thrift with the name IGA Federal Savings Bank. Eight months later the mutual was sold to a private holding, Jade Financial. The chief executive officer of this cooperative and those collaborating with him each received the

amount of \$US 635.000. The members lost all their reserved accumulated over the years, in the amount of \$US15 million.

Once again the question is asked: does the cooperative really need to mobilize external finance for expansion, or it is only that managers claim so. The issue will be discussed in more detail further on.

A different point of view on conversion is brought by Patrick-Mooney and Thomas Gray (Mooney, Patrick & Gray, W. Thomas, 2002). The givens brought by them show that during the ten years prior to the research most of the cases of conversion happened in the cooperative sector, but not all the conversions were from cooperatives to private companies. More than third of these were cases of consolidation by cooperatives, merging among or between cooperatives, joint ventures among cooperatives, and acquiring of private companies by cooperatives.

Looking generally at cooperatives conversions and changes the study found that one quarter of the cases were the enlargement of existing cooperatives without changing the cooperative structure. 15% of the cases were cases of collaboration between cooperatives and stock companies. Only less than 5% of the cases were complete demutualization of cooperatives. Another interesting finding was that cooperatives were three times more likely to have bought stock companies (16.6% of total) than the inverse.

Henehan and Anderson (Henehan & Anderson, 2001) recommend two very important components for a cooperative to be successful, and to avoid conversion:

Common recognition and understanding by members and leadership, concerning the economic problems the cooperative is facing. The second one is also important and is the level and quality of services rendered to members by the cooperative will be better than what each member may achieve working individually.

A major problem that cooperatives face is the lack of finance and capital needed for operations and expansion; this can lead to the assumption that if no solution can be found, the only option for the cooperative is demutualization.

This assumption is linked, in my view, to the fact that a cooperative is established by its members, only when each of the members individually understands that alone s/he would not be able to achieve the service, the products, or employment that s/he looks for, at the cost and quality everyone expects, and because of this they are coming together to create their cooperative.

The problem is that the current approach to capital formation in cooperatives around the world does not link the members to the capital accumulation in the cooperatives. As a result, over the years, the cooperative creates assets and equity, mainly made out of the annual surplus and the retained reserves, without linking the equity to the members who are the source of these resources. This creates a situation in which the cooperative is looking for external sources of funding while the

members are facing the temptation to demutualize their cooperative in order to gain access to assets they have paid for.

Only a cooperative whose leaders understand this fundamental issue, and are doing their utmost to see that all members would get from the cooperative what they look for, can be assured of survival and success. The two researchers Bekkum and Bijman (Bekkum, 2006) refer to this issue. They have reviewed more than 50 cooperatives throughout the world, where new solutions have been developed regarding the issue of capital structure in the cooperative, by collecting data during the last two decades. One of their conclusions is that there are cooperatives which prefer, instead of going into conversion, to safeguard the structure and the identity of the cooperative. They are proposing a new model of cooperative, the publicly listed cooperative hybrid.

On pages 3-7 they review these 50 cooperatives and find the following solutions:

- Appreciable and/or internally tradable shares. The members get an increased real value of their shares, sometimes only partial increase, in the cooperative assets.
- Externally tradable subordinate bonds. These provide a very attractive opportunity to obtain external capital for the cooperative. These bonds may serve as guarantee to outside finance.
- External corporate investors at subsidiary or group level, who may also be members in special standing and are sometimes in accompanying position of the cooperative. This situation may create a possible conflict between member and

investors.

- Public listing of preferred stock. This possibility is preferred from listing of common stocks.
- Conversions into farmer-owned limited liability companies, usually happens in agricultural cooperatives.

The Canadian government's new Cooperative Act has created another form of cooperative, which tries to respond to the problems and the limitations of the actual membership approach in cooperatives (Act, 1998). The May 2007 version speaks about a new form of cooperative, which creates an Investment Share Ownership (ISO) which is valid beside the typical Membership Share Ownership. The ISO is not limited to members only.

Another factor, which was already mentioned above, is the real ownership of the cooperative by the members. In most cooperatives worldwide, based on the current practice and the 3rd ICA cooperative principle, the ownership is a collective and common ownership, and there is no relationship between the real value of the aggregate shares of members - which is relatively very small - and the total real value of the cooperative's assets. There exists a deep and huge gap between these two sides of the equation. This gap, of which members are usually ignorant, creates a situation where members are easily tending towards demutualization, especially when the cooperative ceases to supply the services the members were used to receiving (Galor, 2001b).

Demutualization of Cooperatives in Australia and in New Zealand.

In Australia happened a process of demutualization of housing cooperatives, described by Garry Cronan (Cronan, 2007). These are the Buildings Societies, which are practically mortgage cooperatives. In another paper Garry Cronan (Cronan, 1994) examines why Australian cooperatives have chosen to change their status to Investors Owned Firms (IOF). The main reason why this form has been chosen when demutualized in Australia is because that the cooperative movement in Australia didn't offer cooperative alternatives to cooperatives facing demutualization, among them to remain cooperatives and trying to overcome the difficulties by offering responses to the problems.

It is especially relevant that there was not an appropriate federated cooperative network to offer the necessary backup and support. The cooperative movement in Australia also lagged behind the pace of economic development in other sectors of the country's economy.

Cronan also found that in Australia the primary cooperatives were developed, but secondary and tertiary cooperatives did not.

The history of demutualization of cooperatives in Australia was already underway in the 1950s, and continued during the seventies and eighties. During the seventies many cooperatives conversion took place.

Recent research by Robb and Cromble (Robb, 2006b) found that in the ten years prior to their study the rate of demutualization in Australia went down considerably.

A famous case in Australia of a failed attempt at demutualization is the Connect Credit Union in Tasmania. In 2003 the members of the cooperative were surprised to learn that the management of the cooperative had proposed to list the cooperative at the stock exchange. Those opposed to the management plan got very short time to prepare their opposition.

Those opposed to the proposal started to learn about the issue, received lot of international cooperative support from those with experience on the subject, and successfully informed the members about their findings in time. The proposal was rejected, and the leader of the opponents was elected to lead of the cooperative.

Robb's conclusions comments which may serve other cooperatives facing a similar situation:

- The management of Connect was wrong in its strategy to convert the cooperative when the management was very far away from members.
- The change presentation provoked members opposition.
- The opponents of demutualization were reinforced by knowing the outcomes of former demutualization cases in Australia, which promised much to members but failed to fulfill those promises, while rewarding extensively members of management board and external advisers.
- Objection to demutualization was also demonstrated in the

framework of the communities where members of the cooperative live. A survey of 5000 Australians found that 50% think that demutualization way is wrong, and only 19% think that cooperatives are outdated. This element is important because it shows us that the community can play an important role in avoiding demutualization of cooperatives.

Demutualization can be avoided.

The situation in New Zealand is slightly different than that of Australia. Ian Reid (Reid, 2006) distinguishes between the two neighboring countries. The Australian experience has led them to choose a strong government policy and legal intervention to control the process of demutualization, in order to protect the interest of the community where the cooperative candidate to demutualization in question is located.

In New Zealand the situation is different; the subject of demutualization and how to stop it have no place in the political life. All power stays in the hands of the members, even if the decision is to demutualize the cooperative.

Roger Kerr (Kerr, 1999) analyzes the state of the cooperative movement in New Zealand. He finds that the movement has many weaknesses, which are mainly structural. These weaknesses are especially apparent in dairy cooperatives.

Ramsey Margolis (Margolis, 2007), Executive Director of the New Zealand Cooperatives Association, in an electronic mail

to me mentions that Fonterra⁵, the biggest cooperative for marketing and processing milk in New Zealand, and one of the biggest cooperative of its kind in the world, is facing a strong pressure on its members to demutualize the cooperative.

In 2004 the newsletter of the Canadian Cooperative Association (Association, 2004) published a report about the Fonterra cooperative in New Zealand. The report told that this cooperative is intending to make survey its 12.000 members-farmers before starting any move towards demutualization.

The problem which concerns the members of Fonterra shows us the rise, on the one hand, of the value of the cooperative's assets and a consequent rise in eachmembers share value. On the other hand, there is a decrease in the reward they are getting for the milk they supply to the cooperative.

There are members of Fonterra who think that the cooperative should increase the price the cooperative pays to members for each kilogram of milk supplied to the cooperative rather than accumulate the money in preparation for global expansion of the cooperative business. Other members prefer investment of money towards global expansion and want to change the financial structure of the cooperative towards demutualization.

So far Fonterra has resisted the pressure of demutualization.

Two scholars, Chaddad and Cook (Chaddad, 2000) examine a

5. For more detail on Fonterra see: <http://www.fonterra.com/wps/wcm/connect/fonterra.com/fonterra.com/Home/>

problem found among the dairy cooperatives of Australia. The paper was written following a general meeting of the members where they are about to decide of the fate of their cooperative, after two years that 774 information meetings by the management with the members took place.

The Dairy Farmers cooperative is focused on three major products: fresh milk, cheese and processed milk food. The total annual production in year 1997/98 was above one billion Australian dollars.

The problem in this cooperative came when its leaders judged, as a response to the new situation where the market is unregulated, their cooperative will not be able to continue with only members' own capital. Meanwhile, private industries in the dairy industry are more versatile and have a wider range of financial sources, so their expansion possibilities are easier.

The dilemma in this cooperative was how to balance mobilizing funds from outside of the cooperative, while preserving the control of the members. The Dairy Farmers cooperative studied various models from around the world in which cooperatives faced similar situations. The Irish model proposes that the cooperative create a publicly listed companies (PLCs), through which all the property of the cooperative will be handled, while the cooperative maintains the majority and the control over this company.

However, dilution, in the case of Ireland, of the stock capital of this company reduced members control and ownership below 50%, therefore the Irish model was not sufficient to preserve the member control and ownership of their cooperative.

From 1993 to 1999, there were discussions among the members of the cooperative. In 2000 management of the cooperative brought towards 2000 a proposal to members to adopt a new model, which they called the Equilibrium Model. This model proposes two steps. The first one is the creation of a supply cooperative by the name of Dairy Farmers Supply Cooperative. This cooperative is fully owned by the members-farmers, with each share valued at one Australian Dollar, and not tradable.

Simultaneously, there will be established a cooperative called the Trading Cooperative. In this second cooperative the members will also have full ownership until the cooperative will be listed on the stock exchange. The new proposed situation is that 75% of a member's equity is in the first cooperative and 25% of it is in the second cooperative.

Two years later the second cooperative establishment should start. The share of the second cooperative will be traded at the market, and the value of each member share will change according to the market price.

There exists in Dairy Farmers cooperative a group of members which opposes to this proposal and wishes that the cooperative will simply be converted into public stock company. However, the General Assembly of the cooperative has decided in 2004 (Farmers, 2004) to adopt the first phase of that proposal.

Demutualization of Cooperatives in the USA.

There were not many demutualization cases in the USA during the 1990s, as mentioned by Nancy Jorgensen (Jorgensen, 2005). She raised some questions concerning those demutualized cooperatives:

- Do cooperative members give up their long term good for short terms ones?
- Do demutualization really expand marketing opportunities to the products of the former cooperatives?
- Is it necessary to expand the term cooperative in favor of a broader and different form of producers ownership in their enterprises such as Limited Liability Companies (LLCs)?

She quotes another scholar Mark Hansen, a proponent of cooperative demutualization, who claims that cooperatives are demutualizing for three reasons:

- Increasing cooperative property and acquiring external capital.
- Obtaining financial liquidity.
- Increasing and accessing the value of the business.

He mentions that when agricultural cooperatives succeed, the total value of their produce is lower than the total value of the business itself.

Historically, agricultural cooperatives were created in the USA as a response to the market conditions, and the need arises to coordinate among farmers and to defend their interest

as producers. Two scholars Lois Stanford and Julie Hogeland (Stanford, 2004) explain that these cooperatives were intended to provide small farmers a better and more efficient access to markets, as well as a steady and stable income. During the last two decades various changes occurred in the local market in the USA, mainly because it became open to the global market. This new situation creates a new challenge to the agricultural cooperatives in North America.

The two, Stanford and Hoegland, have learned why the Avocado Growers Cooperative in California Calavo has responded to these changes by demutualization.

The leadership of Calavo proposed a policy, in light of the fact that the total avocado production of the members of the cooperative, as well as the total avocado production of farmers in California, were not sufficient to meet the needs of the avocado export policy. So they moved the cooperative towards disengagement from the best interest of the avocado growers to an organization with global interests influenced by the best interest of the stock holders - to maximum the profitability of what was the cooperative.

This, in the view of the writers, is not the way agricultural cooperative should be run and managed. In their view, considerations such as the welfare of the member and social services to members are very important, even though they may decrease the cooperative profitability. These considerations were ignored by the management of Calavo. The outcome was the demutualization of the cooperative.

Another case of cooperative demutualization is described by

Shermain Hardesty (Hardesty, 2005) . He described the story of the Diamond Walnut Growers cooperative. The general meeting of the cooperative approved a proposal on 1.7.2005 to be merged into an existing stock company.

Hardesty found that the outcome of the demutualization on members varied according to each member. Members who planned to continue to grow walnuts for the next 10 years were expected to loose out in the demutualization because they were going to get worse rewards to their produce. On the other hand, members who planed to cease production immediately found that the demutualization was a good move.

Julie Hogeland (Hogeland, 2006) explains that the main value of the Diamond Walnut Growers was its brand name, and the members believed that utilizing it in the new structure would attract external finance and help to penetrate new markets.

The next cases will describe agricultural cooperatives in California that were closed because of difficulties to adjust themselves and to remain competitive in the market where they operate.

Jennifer Keeling (Keeling, 2004) describes the closing of the Rice Grower's Association (RGA) cooperative. The cooperative closed in 2000 after 80 years in existence. At its peak this cooperative supplied at its peak 70% of the total rice production in California. In the year of its closure it supplied only 5% of the rice of California.

Himawan Hariyoga and Richard Sexton (Hariyoga, 2004) describe the closing up of the Tri Valley Growers cooperative in California. This cooperative had 500 member-

farmers. They produced tomatoes, peaches, pears and olives to be marketed or processed by the cooperative. In 1998 the cooperative sold produce worth US\$782 million dollars. The equity of the members valued at US\$125 million dollars. The cooperative employed 1500 permanent employees and 9500 seasonal workers.

In 2000 the cooperative had to declare bankruptcy under Chapter 11 of the American law, because of financial difficulties. As a result the assets of the cooperative were sold and it ceased to exist.

The reasons for the failure detailed by the authors existed as early as the beginning of the nineties. These included debts which were too high related to the equity of the cooperative, lack of profitability in the food processing industry, and the failure of the financial restructuring plan of the cooperative. Other reasons included excessive payments to members for their produce, and the inability to revoke the membership of non-active members. Another reason was a failure in the marketing plan.

Arguments were raised that cooperatives are not suitable for a competitive market economy. The writers reject this claim and present examples from similar cooperatives in California which continue to operate successfully.

Credit unions are another cooperative branch where attempts have been made to demutualize. David Doss (Doss, 2004) describes a case in which there was an attempt to convert the Columbia Credit Union in Vancouver, Washington, into a mutual saving bank. The vote on the issue of demutualization

took place on an ordinary working day, and only 10.000 members out of 59.000 members took part. The conversion was approved by a majority of 52% of the votes.

The demutualization process was stopped because of an appeal by a group of members who were supported by the National Credit Union Administration (NCUA). They finally forced the Washington State Secretary of the Treasury to investigate irregularities in the vote. The vote was voided as well as the demutualization.

Proponents of the conversion claimed that demutualization would be favorable to members, especially in terms of tax exemptions gained. It was found later that the pressure for conversion came from members who had larger accounts in the cooperative, and hoped to get a greater number of shares from the new corporation.

NCUA also discovered that those who promoted demutualization concealed information about their plan to continue and to turn the mutual into an ordinary commercial bank.

Another aspect of the cooperative life in the USA was examined by Brian Henahan (Henahan, 2002). The research took 10 years, between 1989-99, and examined 50 cooperatives mergers. Among them 40% were dairy cooperatives. The research found that the factors in favor of mergers of cooperatives are: integrating of managements; reducing processing, marketing and operating expenses; avoiding competition among cooperatives; and seeking higher returns for members. This research showed that the merged cooperatives showed

better results than before the merging.

There have not been many demutualizations in the USA, but the economic pressure towards demutualization brought threats to change the cooperative law. These are the findings of research done by Taylor (Taylor, 2004) about demutualization. The research suggests adopting the approach that the best defense is the attack, and by saying this Taylor recommends the creation of structural tools to make difficult such a move, and sometimes to prevent or halt it.

The recognition that external assistance is needed by a cooperative when facing pressures of demutualization led the management of Credit Union National Association CUNA (CUNA, 2005) to adopt these very important recommendations. CUNA supports and forwards any form of protective legislation on the state levels as well as a charter defining the whole credit union movement.

The measures taken enabled the adjustment of the statutes of cooperatives to ensure that members fully understand the meanings of the demutualization. This institutionalization of a mechanism of public discussion for members before any vote could take place. They also created a liaison mechanism between members opposing demutualization and the rest of the members. Stronger transparency for members ensures that they understand entirely the effects demutualization.

CUNA has taken upon itself the steps to educate members of

credit unions concerning the cooperative identity. This includes how credit unions are different from other economic enterprises, such as the fact that members are the owners of their cooperative.

Demutualization of Cooperatives in Canada

The situation of cooperatives in North America in general, and in Canada in particular, has changed considerably, as described by Murray Fulton and Al. (Fulton, 2006). The agricultural sector was beaten down hard, when many big cooperatives have declared bankruptcy or demutualized.

At the same time, a wave of new generation cooperatives - (NGGs) were established, especially among agricultural food processing cooperatives; these have a different ownership structure.

Many savings and credit cooperatives have gone through the consolidation process. The consumers cooperatives and their second level cooperatives for wholesale and marketing underwent a severe crisis, and in many cases disappeared. Only cooperatives that specialized in niche markets such as organic food have been successful. This was the case for the cooperative SPIN (SPIN Farming & 2007,) which was established in the town of Saskatoon, Saskatchewan. According their website, this model has been extended to the Canadian provinces of Ontario and British Columbia.

During the period between 1998-2002 the number of agricultural cooperatives that have been converted has increased, especially in Quebec, and especially among cooperatives for agro-processing (Gurung, 2005). There was a decline of 26% in the production made by agricultural cooperatives in Canada during the these 4 years.

Another sector facing increased demutualization in Canada is that of insurance and mutual health cooperative (Anthill, 2006). The history of these cooperatives in Canada is long. The first mutual was established in the year 1875, and called the Red River Valley Mutual Insurance Company. Today this mutual has more than 44.000 members and its annual revenue from premiums is more than C\$23 million.

What are these mutuals and how do they differ from cooperatives? The following explanation brought in the article above:

"A mutual is a voluntary group of individuals who derive joint benefit from sharing risk."

A mutual is defined by the fact that it provides an intangible service to its members - the division of risks among the members. A cooperative supplies to its members a tangible service. A mutual does not exist to make propfits, so the total profit is reinvested in the mutual itself, to ensure more effective insurance to its members. Practically, this is the reason why so many have tried to demutualize them since the prospective "loot" is high.

The mutual doesn't offer shares to members, but they have an insurance policy. The members have no right to get anything out of profits. Members can't sell shares since they don't have

them, and this presents another difficulty to dissolution. This is the reason why demutualization has been chosen.. The article explains:

"Demutualization is a process whereby a mutual sells ownership to those who buy shares."

In Canada demutualization has many supporters. They have tried to promote the idea with the argument that this move will help mobilize external finance and will enable competition in the world market.

The paper cites Jonathan Michie who wrote in his paper "New Mutualism A Golden Goal" that:

"The impetus guiding demutualization is driven by the short-term desire to consume the mutual cake and make a profit; however, once the mutual has been digested so too are its benefits for future generations."

In order to encourage and to regulate the demutualization the Canadians passed have enacted in 1999 an act which permits a mutual to demutualize and, sale shares to the public. Following the act, four of the largest mutual of Canada were demutualized. After this, Canadiana mutuals remained only in the domain of property and damages. At the same period of time, the government of Canada enacted a law putting many limitations on demutualization. The government originally presented a description of the proposed act on its website in 1998.(Department of Finance, 1998) a description of the 1999 act proposals.

The proposal itself, even before being adapted by the Canadian parliament, provoked a response (CONSULTATION

PAPER, 1998) which included some technical steps to amend this insurance act, which was then in process of being enacted.

The proposals:

- Called for a longer time to notify members about a coming general meeting discussing the issue, and to ensure that owners of the policies are well informed about the demutualization proposal.
- Ensured that only valid policy holders participate in vote.
- Enabled the transfer of liquid assets from the current accounts to the accumulated funds, in order to increase the value of the mutual, and distribute to the actual valid policy holders.
- Increase government control over the process of demutualization.

As mentioned above, the agricultural sector was the most affected by the demutualization of the cooperative Saskatchewan Wheat Pool, which was established 80 years ago, when wheat growers decided to cooperate to be able to escape from those exploited them. The cooperative decided (Lord, 2005) that the control of the cooperative would be transferred from the 73.000 members-farmers into the hands of investors and share holders.

Demutualization in the European Union.

If we examine the demutualizations which took place among cooperatives in Western Europe and especially the countries

which are members in the European Union, we find that the phenomena was similar to other part of the world where demutualization occurred. Nevertheless, we shall be able to observe and discuss a few new characteristics in this process.

The demutualization process, which received special attention in Western Europe, started already at the beginning of the nineties. The article of Johnston Birchall (Birchall, 1998) tells that Great Britain led during this decade the demutualization of cooperatives to stock companies during this decade, with the most pain felt among the friendly societies. By the end of this period the number of friendly societies which hadn't demutualized were only 30% of their number ten years earlier. Many in Britain claimed that the cooperatives would disappear. But, the reaction was on the contrary. In 1998 only one cooperative of this sector was under threat of demutualization. Medical insurance mutual's were also at high risk of demutualization. Statistics show that at least half of them are under the process of demutualization.

Another sector where demutualization took place is the agricultural cooperatives, Among the agricultural cooperatives 2 out of 4 went demutualization, especially those for the marketing of milk. These cooperatives are dominant in the agro-industrial sector. The following article (Enright, 2005) deals with the subject examines the situation of various cases of concentration and internationalization of these dairy cooperatives. Many of these cooperatives have been converted into international structures. This situation resembles what is hap-

pening in New Zealand with Fonterra, described above, and the recent case of the Israeli cooperative Tnuva, which will be discussed later on.

The Association of European cooperatives and mutual insurers has prepared a long report on the demutualization of insurance cooperatives (ACME, 2001). The central arguments for the demutualization were mainly based on the belief that this process will bring an increase in efficiency, more accessibility to financial resources needed for expansion, and an increase in business flexibility. Another argument was that demutualization brings more profits and therefore more advantages to directors, to the employees of the mutuals and to the share holders.

The research sought to examine these arguments. It checked 97 mutuals from 11 West European countries, and which represented 24% of the total premiums in the West European insurance market.

The conclusions of this research were that the arguments for demutualization were in most cases unfounded, were based on unproven facts, and were more based in ideology than reality. The study showed that insurance cooperatives are competitive, consumers oriented, and in most cases showed better performances than those who gone through demutualization.

Another domain where demutualizations in their broad scope took place is the credit unions. In a study made in Ireland, Ella Kavanagh (Kavanagh, 2005) examines the saving and credit

societies for farmers founded in Ireland since 1894. They have been established according to the Raiffeisen model from Germany. The movement developed and at its peak in 1908 included 267 societies. Their number decreased gradually and reached 35 societies in 1935. One of the reasons for this decline was the competition these cooperatives faced from other financial institutions, like the banks or the postal bank which also accepted saving.

The study checked the problematic quality of management in these cooperatives, as part of the causes for their disappearance. Another problem mentioned in the study is the high fees these societies charged the members, and the high rate of interest on credit to their members. As a result, the demand for these loans decreased and they became less common.

As a follow up of this subject, and providing a contrary example, it is important to note the situation of credit unions in Ireland today. Raymond O'Connor & Olive McCarthy (O'Connor, 2005) describe how these cooperatives have been developed very nicely from the end of the 1950s. In 2000 these cooperatives counted 2.6 millions members with total savings of 5.7 billions Euros. The secret of their success is found in the various communities mainly in rural areas, where they are, and the good links they have been able to develop with these communities. This cooperative movement has developed well within its socio-economic and cultural context.

A cooperative network for agricultural credit exists in Portugal. Portuguese Agricultural Credit Cooperatives (PACCs)

was studied by Paula Cabo and João Rebelo (Cabo, 2005). This cooperative movement fulfilled a very important role in the banking system in Portugal, especially for the agricultural sector in the country, and it is the second-largest system in the country.

The movement is now facing these days survival challenges which developed from difficulties in mobilizing sufficient self equity capital from its members. The main source of further finance was always the undivided accumulated reserve funds. The study observes that the federation attempted to intervene in the management of certain cooperatives by the appointment of managers out of these cooperatives, but this did not bring about the expected results. The management operating expenses were too high.

The cooperatives were declared by the European Union, the United Nations and the International Labor Organization (I.L.O.) as a means to create employment and to mobilize necessary funds. In spite of that, Josefina Guadaño, (Guadaño, 2004) describes a tendency towards demutualization among cooperatives in Europe. This process happens as a response to the globalization and the increased competition. The outcome of this situation includes an increase in the number of cooperative mergers and in the mobilization of external funds by the cooperatives. The writer claims that these two trends reinforce the cooperatives economically but weaken their identity and links to the cooperative principles, thereby weakening the cooperative and exposing it to demutualization.

Another sector in Western Europe where demutualization took place is cooperative banking. In a study published in Canada, Benoît Tremblay and Daniel Côté (TREMBLAY & CÔTÉ, 2001) are examining cooperative banking demutualization. They emphasize the case of the cooperative bank CERA in Belgium that was merged with the cooperative bank Kreditbank, which they claim was motivated less by a need for capital than by the need for strategic positioning in response to consolidations in the banking system in Belgium and the merging of two big private banks in this country. The merging of these two cooperative banks into a new one - non-cooperative, created an economic body controlling 25% of the banks in Belgium and 10% of the insurance market there.

The main comment of these researchers on the subject is that the current capitalization of the new bank is the outcome of assets accumulated by generations of cooperative members.

Their research also focuses the discussion on the process experienced by four additional cooperative banks went through in Western Europe.

The first one is the Crédit Agricole from France. The bank counts today 2672 local societies, which are organized in 48 regional funds, and these regional funds are in turn organized as the National Federation For Agricultural Credit (Fédération Nationale du Crédit Agricole (FNCA) and la Caisse Nationale du Crédit Agricole (CNCA)).

In the different funds there are 5.5 millions members who elect 35.413 managers on the various levels. The local societies contribute the capital of the regional societies and these re-

gional societies contribute 90% of the capital of the national fund. The fund hoped that its listing on the stock exchange would help to stop demutualization processes, and the capital thus mobilized would finance their international expansion.

This policy to maintain its cooperative structure, as they hope, will acquire full or partial control and ownership on private banks. They have acquired the Indosuez bank; as well as partial ownership on Banca Intenso in Italy, Crédit Lyonnais, Banque Commerciale in Greece, Impériale de Lyon Bank, and on BES (Banco Esperanto Santo) in Portugal. FNCA/CNCA also bought a controlling share of ELF crédit-bail immobilier in Poland. The bank also has links to companies for consumer credit and to companies which offer life and property insurance.

This formula of Cooperative - Capitalistic enterprise is a challenge and at the same time a call and an opening of a door for demutualization. The writers think that demutualization is not imminent but possible on the medium and long term term, especially because each time a need for supplementary capital arises that, will dilute the cooperative part of the fund.

The next cooperative bank discussed in that paper is the Rabobank in Holland. This bank includes a network of 400 local cooperative banks having 700.000 members and serving 9 millions clients. The bank was established in 1972 whit the merger of two networks of cooperative banks. The new unified group succeeded and grew as a result of this merger. A major practice of this bank is to keep all surplus in reserve funds which helps the group to continue to greatly expand its

economic activities.

In the middle of the nineties the bank formulated the new statutes intended to keep the bank out of demutualization.

In the mid-1990s, these extra funds provided the resources for successful business activities in the international market. The bank is concentrating in the agri-food sector and they have set a goal of 4% of world market share. The second focus of its international activities is expanding its activity towards the development of cooperative banks. One of the first collaborations was with the German cooperative bank DG Bank (banque centrale du réseau coopératif allemand), but that experiment failed. Nevertheless, the Rabobank is looking to create an European Cooperative Bank.

It continues a policy of enhancing its cooperative basis. In year 2000 it distributed certificates of participation in investment (certificats d'investissement) at the value of 25 Euro each and which were sold only to members and to employees of the bank, and which paid one percent of interest over the interest paid by the government of Holland on bonds. This distribution has been a great success, resulting in 210.000 new members joining as results, and the goal was to have one million supplementary members in year 2003.

The third cooperative bank surveyed (TREMBLAY & CÔTÉ, 2001) was the Belgium CERA bank. In this case, mentioned above, the merger with Kreditbank cooperative in 1998 led to the creation of a new private bank called KBC, which is a stock company in which CERA has 40% of the shares, but

maintains its cooperative status.

Before the merger CERA was a typical cooperative bank, including 207 local banks with 907 branches, owned by 410.000 members and serving 1.500.000 clients.

Even though CERA was officially a cooperative, in reality members didn't have a sense of their identity as members of a cooperative. This was probably a main reason behind the demutualization decision of CERA. Members' reaction to the demutualization proposal was positive, and they negotiated only to increase their share in the property of the cooperative, when the initial decision was to give members the nominal value of their share.

It is important to note here that this decision is a logical outcome of the ICA practice and the third principle done around the world. Members shares are kept in their nominal value, and as we have seen above, brought to ease the demutualization from the members point of view.

The conversion of CERA and merger with Kreditbank created in Belgium, which covers 25% of the market and 10% of the insurance market. The bank also moved toward international investment, especially directed to Eastern Europe.

The fourth bank in this research (TREMBLAY & CÔTÉ, 2001) is the Co-operative bank in Great Britain. Unlike the previous three cases, this bank is not a cooperative bank but rather a subsidiary and fully owned by the world's first consumer cooperative, Rochdale, England's, Consumer Wholesale Society (CWS). The directors of this bank are members

of the consumer cooperative. The bank is jealously preserving its cooperative heritage and contributes 3% of its gross revenues to local communities.

The bank excels in quality of service to clients. It defines that the stakeholders are responsible including members, employees of the bank, suppliers, local communities, the environment and the past and future generations.

The writers are trying to arrange these four banks along an axis between cooperatives (Intensité des règles coopératives) and the market economy (Intensité des règles de marché). On this axis the cooperative bank of Britain is the closest to the cooperative end, followed by the Rabobank of Holland, the French Crédit Agricole, and finally the CERA bank of Belgium being most market oriented.

Another example of cooperative banks in France which created stock companies, is the example of the **Credit Mutuel of France** which can be found here (Mutuel, 2006). This cooperative bank was established in 1882 in Strasbourg and influenced by the German model of Raiffeisen. In 2005 this was the third largest bank in France. The bank is divided into three levels. At the local level it includes 1800 local funds. At the regional level there exist 18 regional federations, and all of these are members of the national federation.

This cooperative bank established a CIC - a special holding (holding du groupe et banque de réseau en région parisienne,) (CIC, 2006) which is based in the Parisian region, but engaged in vast international activities.

Two cooperative banks, the Caisse d'Epargne (d'Epargne, 2006) and the Banque Populaire have joined forces. The Caisse d'Epargne bank included 440 local saving cooperatives, having 3.4 millions members. These members own 80% of the shares of the Caisse d'Epargne.

These two cooperative banks have established a stock company named NATIXIS (NATIXIS, 2006). This new company offers the following bank services: banking and investment, private banking, assets management, bank services and income management. Each of the groups owns 34.4% of Natixis, which has 23.000 employees, one third in France and the rest in 68 different countries.

Johnston Birchall (Birchall, 1998) tries to draw some conclusions out of this situation in order to help avoid demutualization. A main point to consider and to know is the ability of the cooperative to redefine the ownership relations and the way this ownership is realized in the cooperative. A further point is to find ways to reward members for their participation and especially how to encourage them to participate actively in the decision-making process. These steps may assist the revival of cooperatives in Great Britain. He writes:

"If mutuals and co-operatives do succeed in redefining what it is to be a member-owned business, and do find ways of rewarding members and involving them in decision-making, then there is the potential for the emergence of a real 'third sector' with its own ideology and distinctive place in the market."

Demutualization in South-East Asia.

The material on this region is quite limited. Only some internet resources are available.

In the year 1970 the trade unions in Singapore the NTUC - National Trade Union Congress decided to create the - **Comfort Taxi - Singapore**, a cooperative which organizes the taxi drivers in this country. (Singapore, 2006) The cooperative has been described by its founders as Workers' Cooperative Commonwealth for Transport Limited. The aim was to create a better working environment for taxi drivers, as well as employment and income. In 1992 the cooperative was converted into a stock company listed on the stock exchange of Singapore. The new company knew a lot of success.

Bank Bukopin (Bukopin, 2006) in Indonesia has existed for 30 years. The bank was established as a cooperative bank, but went into demutualization and became a stock company in 1993. The Indonesian Batik Co-operative Association - also known as GKBI went into demutualization and is no longer a cooperative. (suroto, 2007)

In Sri Lanka there is a case of demutualization mentioned by Mr. Nair from the ICA-APRO (Nair, 2007). He describes the federation of saving and credit cooperatives in Sri Lanka, the Sanasa. This federation is 100 years old and includes 8400 primary societies. It is described in this report (CANADIAN, 2007) . The Bank of Sanasa was established in 1997, and the

clients are the primary cooperatives, which are the members of the federation, as well as 200.000 private clients. The federation (Kiriwandeniya, 2006) has also founded Sanasa Consumer & Producer Alliance company - which linked between producers and consumers - a campus for higher education, and a stock exchanger brokers company.

Demutualization in India is discussed by Prabhu (Prabhu, 1999) and is focused on the cooperative banks in this country. The central issue these cooperatives are facing is their ability to preserve the ICA cooperative principles. This stance is in possible contradiction with the need to raise funds in the private or public market. The writer thinks that doing so in the market without giving these funds any rights of ownership in the cooperatives is possible, provided that the cooperative bank is supplying to the investors the necessary credibility, and when this approach lessens the pressure towards demutualization.

The Demutualization in Israel.

The cooperative movement started in Israel at the end of the nineteenth century. There exist in Israel many forms of cooperatives in various branches of activities. Some of them are unique to Israel, such as the Kibbutz, the Moshav, the Moshav Shitufi, and all the socio-economic structures established by them.

The cooperative movement in Israel has gone through many

difficulties during the last two decades of the twentieth century.

The savings and credit cooperatives, in the form known in other countries around the world, were first established in this country at the beginning of the twentieth century. The description of the development of these cooperatives is provided by Zvi Galor (Galor, 2000), in an essay which goes on to describe the end of these cooperatives. This end is similar to the demutualization process known in other countries, beside the fact that it happened during the sixties and the seventies.

The consumer cooperatives movement has played an important part in the retail consumers market, and is described in Galor (Galor, 1986). A description of the demutualization some of them have gone through is given by Galor (Galor, 2000). This is a classical case where a very large cooperative called Blue Square was demutualized into a public company. The cooperative was based on the common structure and ICA principles for many years of existence and thanks to this principle and the practice it imposed on, brought that the members owned only few percent of the assets of the cooperative. The demutualization provided each members with a return of approximately US\$ 20000.

Tnuva, the secondary cooperative for marketing agricultural produce has gone a prolonged process of demutualization which prolonged during the last decade, (Galor, 2000) and as of the middle of 2007 it has not been finalized (Galor, 2006).

Another cooperative which has demutualized and a broad discussion on it would come in a different chapter is the public transport cooperative Dan in Tel Aviv. (transport, 2007). The cooperative was established in 1945 out of a merger of two other public bus cooperatives that operated in the region of Tel Aviv.

The cooperative became a stock company in 2002, and is now the second-largest in Israel in this field of activities.

One of the original forms of cooperatives in the world is the Kibbutz. The Kibbutz has undergone many changes in the last 20 years, which would be described in another chapter, but it is important to note here that the Kibbutz is an interesting form of rural community, which is based on agriculture, but includes non-agricultural employment, and especially industry. The portion of Kibbutz revenue from industry has surpassed those from agriculture (Galor, 2001a).

A very interesting step taken by the Kibbutz was the extending of the economic basis of their industries, and the price of this was that part of the ownership is now at the hands of private investors. It is important to note that kibbutz industries that are divided in ownership, are subsidiaries companies, so the private investors have no stake in the Kibbutz itself.

A broader discussion in demutualization in Israel will come in coming chapters.

Conclusions and Summary.

I would like to end this discussion with some comments and conclusions derived out of it. This indicate some directions to expand the discussion on the various issues raised above.

It is important to identify the various components of demutualization as it defined in our study. I'll try to find common elements and those which are missing.

The elements which I found in the definitions:

- Changes occur in the structure of the cooperative from member ownership to investor ownership.
- The cooperative identity is lost, which opens the door to demutualization.
- The demutualization process changes the basic focus of the cooperative, in order to achieve profits, which are the values preferred by the converters.

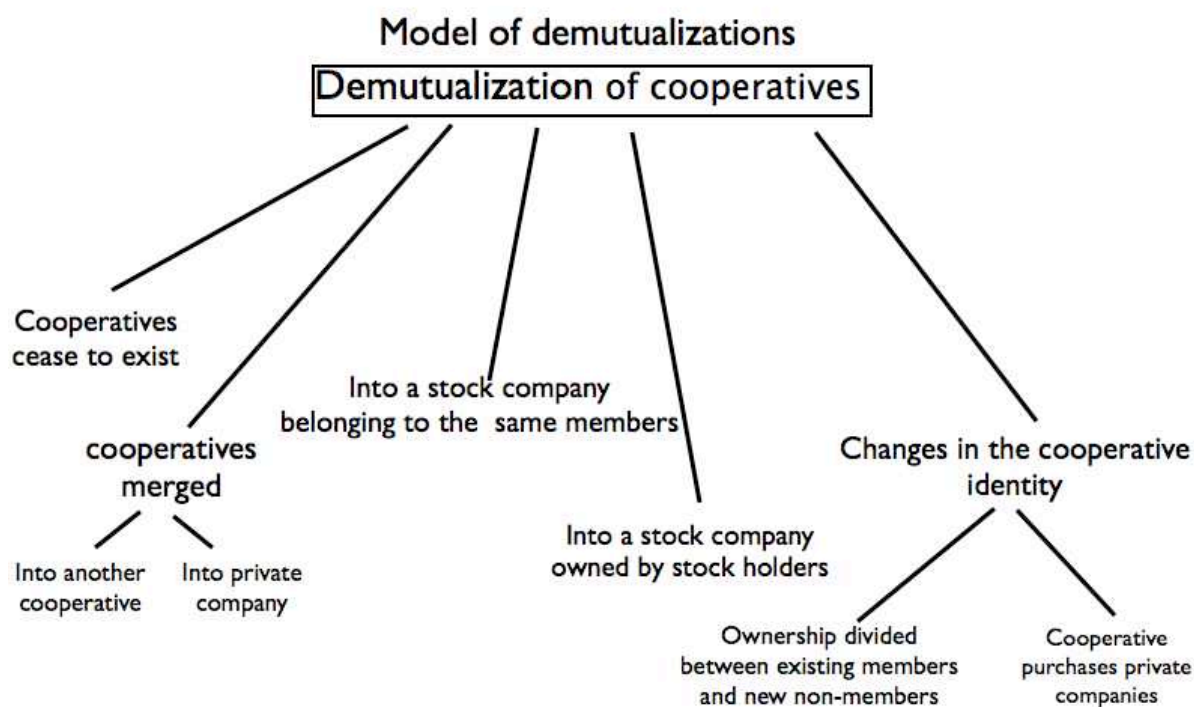
The existing definitions in our study do not refer to the relationship between the members and the cooperative created by them, and from which they expect to get the certain services.

There is also no reference to the gap, sometime very deep, between the very low percentage of equity of members in the cooperative and the total of the cooperative equity.

We shall attempt now to identify the various elements of the

demutualization phenomena:

Chart 1: Model of types of demutualizations



The process of demutualization or conversion happens when a cooperative ceases to respond to the expectations of its members, those who established it and those who are actual members: It fails to supply them with the service or product, for which they have established the cooperative or join to, at the cost they are ready to pay and of the quality they seek. The process may lead the cooperative facing one of these possibilities:

- Demutualization of the cooperative and the end of its existence. The members get what was paid for the rest of the value

of the cooperative, and generally a very modest return. (Munkner, 1999).

- Demutualization of the cooperative occurs when the cooperative is merged into a bigger economic entity, be it another cooperative, or a public or private company.

- Demutualization of the cooperative which continues its existence as a stock company owned by the same members.

- Demutualization of the cooperative which continues its existence as a new entity owned by parties others than the former members.

- Demutualization that otherwise changes in the identity of the cooperative including:

- a. The ownership of the cooperative is divided between its members and new non-members owners.

- b. The cooperative itself purchases private companies either fully or in part .

All these demutualization cases arrive mainly, but not only, in cooperatives where the members and the management of the cooperative do not understand what is a cooperative, do not receive adequate and ongoing cooperative education, and are lacking the understanding of the cooperative identity, and what differentiates a cooperative from other commercial businesses. On the other hand, in cooperatives where members were highly involved in the cooperative activities, and participate in the management of the cooperative, the chances of demutualization are very low.

I did not find cases in the literature where cooperatives whose

members are the real and complete owners of their equity will resist better to demutualization influence. This point will be studied further more.

One important factor helping cooperatives to withstand demutualization is the cooperative environment in which the cooperative find itself. Cooperatives that are members of active and strong federations are more protected and more likely to resist demutualization.

There are internal and external factors to demutualization.

Chart 2: Internal factors

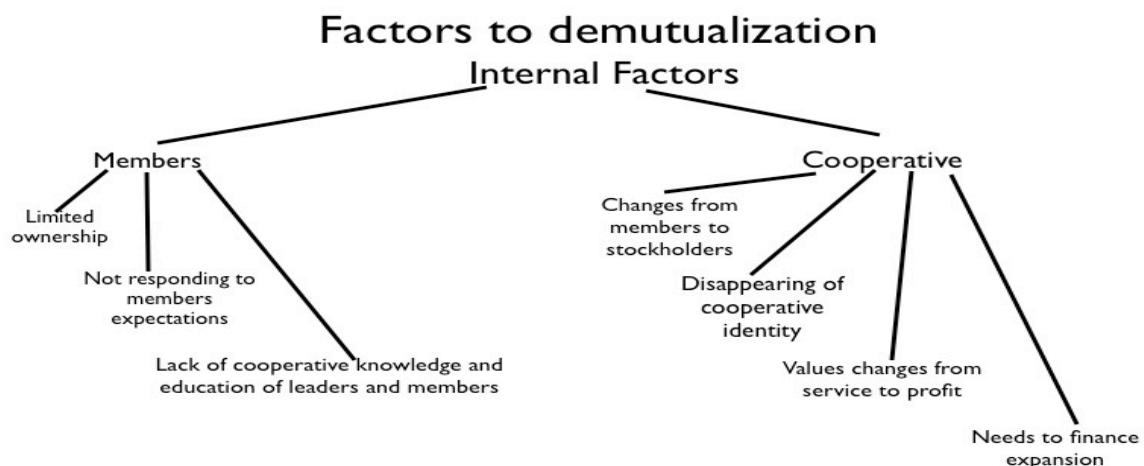
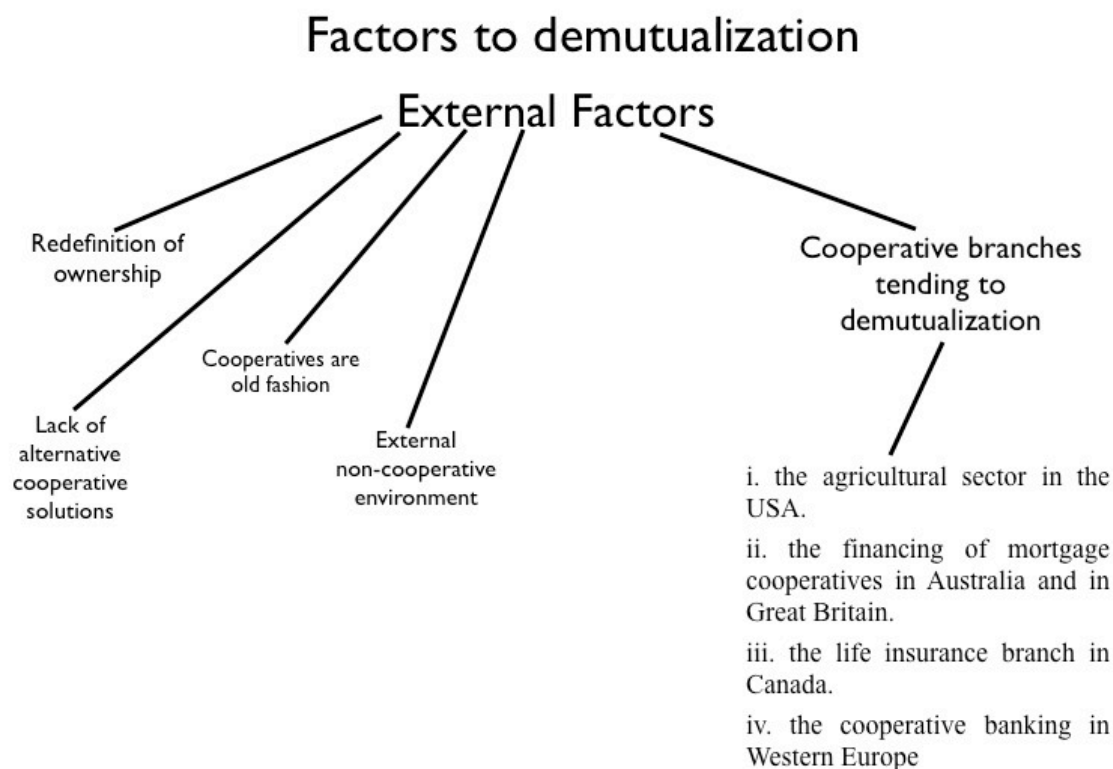


Chart 3: External factors



Among the internal factors we can identify the growing gape between members on one hand, and the board of directors, employees and management of the cooperative, on the other hand. It was found that in many of the cases when cooperatives demutualized, the pressure came from the managers and the directors of the cooperative who were hoping to receive a nice financial reward from this move.

Another internal factor is the lack of continuing cooperative education for everyone, including wage-earners, managers, members of the boards of directors and the members themselves.

One of the major arguments for conversion of cooperatives to another organizational structure is the need to finance the ex-

pansion of the cooperative's operations on one hand side and the inability - and sometimes the lack of willingness or understanding - by members, to supply this needed finance.

The supplementary finance can be acquired in various ways, and not only by demutualization. Various solutions have been applied in different countries, and they have been presented above.

Demutualization of cooperatives has happened in various parts of the world. The literature has addressed the issue beginning in the middle of the eighties with the demutualization that took place in Australia. Apparently, the building societies there were converted because of some inherent weaknesses, such as the lack of alternative cooperative solutions, and the lack of a supportive federated cooperative network that could have supported these alternative solutions.

The most salient characteristic of these building societies was a framework in which there were many members and lot of assets, but the property didn't belong to members. This weakness also characterizes the friendly societies when converted in Great Britain.

Additional demutualization cases in New Zealand highlight the issue of the large gap between the members' ownership in the cooperative, as reflected in the value of members shares, and huge value of the cooperative's assets and equity. The members see themselves as the real owners of this property without real evidence for it.

The existing literature does not provide sufficient discussion of the issue of this gap, and mainly not for the reason behind to this situation: the third ICA cooperative principle and the current practice on the issue in most cooperatives worldwide. The pressure puts on members of the Fonterra cooperative in New Zealand by potential buyers of the cooperative is based on this gape, namely the one existing between the very low members equity value in the cooperative and the very high value of the cooperative equity. Similar pressure by buyers on members can be found in the Dairy Farmers cooperative in Australia. The solutions proposed for this cooperative, as well as solutions offered in other cooperatives, helped to avoid demutualization while responding to the pressure on members.

The demutualization which took place in North America also teaches us some lessons:

- Many of these conversions occurred in the agricultural sector.
- The most common explanation for demutualization was that the cooperative is not an organization suited to the competitive market. A false argument since experience with other similar cooperatives at the market and at the same environment shows full success in their operation.
- Cases where cooperatives have merged without converting showed better financial results than the situation prior to merging.
- The creation of the New Generation Cooperatives - NGCs, most of them in the food processing industry, and their partic-

ularity is the different ownership structure.

- The most accentuated conversions in Canada were in the mutuals branch - the life insurance activity.

Demutualization in Western Europe had various components, including some which already been discussed in regards to other parts of the world, as well as some new elements. The most vulnerable for conversion were the friendly societies in Great Britain, in which resembled the experience in Australia with the building societies, and the health mutuals, in which had experiences like those found in Canada.

Interesting conclusions can be derived from these demutualizations, calling for a redefinition of the ownership relationship between the member and the cooperative, and the ways members are rewarded for the participation in the cooperative. These two changes are the main points utilized by those who are against any change in the current 3rd ICA principle. Peter Yeo (Yeo, 1994) raises the argument that the cooperative is safeguarding the property accumulated by the cooperative over generations, so current members have no right to change the existing relationship between members and their cooperatives. This view expressed the situation that existed in Great Britain, and which consequently brought the various crises described above.

Another domain where conversions took place was in cooperative banking in Western Europe.

We can observe that the development of these cooperatives

were cases of cooperatives ownership of private companies, cases of cooperatives demutualized into private companies, and cases of cooperative banks which create together a new private financial company to run multitudes of businesses.

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