Senate Inquiry

Raising capital in mutuals
An opportunity for political action

Introduction

Australian mutuals are owned by their members, rather than external shareholders. They raise capital by retaining earnings, which means that it is accumulated patiently, over time.

Mutual businesses operating in the financial services sector are unable to raise share capital from their customer members. Credit Unions, Building Societies, Friendly Societies, Mutual Banks and Mutual Insurers have no mechanism to attract investment from their members. This contrasts with the most successful co-operative banks and credit unions in the world, where it is routine for members to invest in the business that they own.

For example, co-operative banks in Germany (Volksbanken) raise more than 10% of their capital from member investments. Desjardins Group in Canada, one of the most successful credit union groups in the world, routinely offers co-operative shares to its members who contribute on average $2,000 CAN each.

In the UK, Parliament has recently passed new legislation to permit friendly societies and insurers to issue shares to their members, opening up the opportunity for meaningful relationships between these firms and their owners, where the success of the business is shared.

As a result, these countries benefit from thriving co-operatively owned financial services sectors, which provide competition and choice in the market place.

The experience of the GFC showed such firms to be more resilient than their stock market listed counterparts.

Australian Parliamentarians have the opportunity to emulate the business environment in which mutuals are thriving, at the same time as creating the mechanism for deeper member engagement in mutuals.

The time has come for new legislation to enable Australian mutuals to open up the potential for their members to be able to invest in the business that they own.

Senate members could recommend that action is taken to pass a new 'Mutual Capital Bill' to bring Australian law up to the standards of the best across the world, and help grow the Australian owned financial mutual sector.

UK Case Study – Mutuals Deferred Shares Act 2015

In March 2015, the UK Parliament approved landmark legislation for friendly societies and mutual insurers to permit them to issue share capital for the first time.

These financial services mutuals conduct insurance and savings business in the interest of their members, but they currently have no share capital.

They raise working capital through retained earnings over time and some issue debt in the form of bonds. In a business environment that expects minimum levels of capital adequacy and liquidity, this means that such member owned firms are at a disadvantage to their stock market listed competitors, which have separate investor share capital.

Deferred shares will enable individuals and institutions to invest in mutual businesses, providing new funds for:

- tactical acquisition and growth strategies
- innovation in new investment areas
- new relationships with members
- new product development
- alternative strategies to demutualisation

The Mutuals' Deferred Shares Act deals with the challenge of how to raise additional external capital in a co-operatively owned business, whilst maintaining its core mutual purpose of providing the best service and quality for the member owners.

It complements changes made to Building Societies legislation in 2013, to enable similar shares to be offered to institutional investors.

In drafting the legislation we ensured that:

- New deferred shares are permanent
- They confer membership on the holders
- No member would have more than one vote as a result of holding the shares
- Investing members that did not trade with the business would be excluded from any member votes related to mergers or dissolution

In addition, it has been agreed with UK Regulators that deferred shares will qualify as tier one (highest quality loss absorbing) capital in the regulatory assessment of the strength of these financial institutions.

Mutuo is currently working with HM Treasury and Regulators to help draft the regulations that will govern the first share issuance, expected in 2016.