

The Senate

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Economics

References Committee

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Cooperative, mutual and member-owned firms

March 2016

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# Table of Contents

<b>Membership of the Committee .....</b>	<b>iii</b>
<b>Terms of Reference .....</b>	<b>vii</b>
<b>Abbreviations and Acronyms .....</b>	<b>ix</b>
<b>Recommendations .....</b>	<b>xi</b>
<b>Chapter 1.....</b>	<b>1</b>
<b>Introduction .....</b>	<b>1</b>
Conduct of the inquiry.....	1
Structure of the report.....	1
Term of reference (b)(iv) - Comparisons between mutual ownership and private sale of publicly held assets and services .....	2
Notes on references .....	2
Acknowledgements .....	2
<b>Chapter 2.....</b>	<b>3</b>
<b>Cooperatives, mutuals and member-owned firms.....</b>	<b>3</b>
Table 1.1 – Types of cooperatives and mutuals .....	4
Definitions .....	5
The scale and extent of the sector.....	9
Table 1.2: Overview of member owned businesses .....	10
Figure 1 .....	12
Table 1.3 Top 100 Australian Co-operative and Mutual Enterprises .....	12
Current state and federal legislation governing co-operatives and mutuals.....	15
<b>Chapter 3.....</b>	<b>19</b>
<b>The barriers to growth, innovation and competition.....</b>	<b>19</b>
Recognition of the contribution and potential of co-operatives and mutuals .....	19
Recognition of mutuals.....	26
Establishing a co-operative.....	31
Issues affecting Indigenous co-operatives.....	37
<b>Chapter 4.....</b>	<b>41</b>
<b>Regulation and access to capital.....</b>	<b>41</b>

Regulation.....	41
Accessing capital .....	45
<b>Appendix 1 .....</b>	<b>53</b>
<b>Submissions received .....</b>	<b>53</b>
<b>Answers to questions on notice.....</b>	<b>55</b>
<b>Tabled documents.....</b>	<b>56</b>
<b>Additional information .....</b>	<b>57</b>
<b>Appendix 2 .....</b>	<b>59</b>
<b>Public hearings.....</b>	<b>59</b>

# Terms of Reference

On 2 March 2015, the Senate referred the following matters to the Economics Reference Committee for inquiry and report by 14 May 2015.

- (a) the role, importance, and overall performance of cooperative, mutual and member-owned firms in the Australian economy;
- (b) the operations of cooperatives and mutuals in the Australian economy, with particular reference to:
  - (i) economic contribution,
  - (ii) current barriers to innovation, growth, and free competition,
  - (iii) the impact of current regulations, and
  - (iv) comparisons between mutual ownership and private sale of publicly held assets and services; and
- (c) any related matters.





## Abbreviations and Acronyms

ACMI	Co-operative and Mutual Business Index
ACNC	Australian Charities and Not-for-Profit Commission
ADIs	Authorised Deposit-Taking Institutions
APRA	Australian Prudential Regulation Authority
ASG	Australia Scholarships Group
ASIC	Australian Securities & Investment Commission
AUCLA	Australian Uniform Co-operative Laws Agreement
BCCM	Business Council of Co-operatives and Mutuals
BusVic	Bus Association Victoria
CAANZ	Chartered Accountants Australia New Zealand
CCUs	Cooperative Capital Units
CENREC	Central New South Wales Renewable Energy Co-operative Ltd
CERU	Co-operative Enterprise Research Unit
CMEs	Co-operative Mutual Enterprises
CMMOO	Co-operatives, mutual and member-owned organizations
CNL	Co-operatives National Law
COAG	Council of Australian Governments
COBA	Customer Owned Banking Association
CPSU	Community and Public Sector Union
EY	Ernst and Young
GFC	Global Financial Crisis
IASB	International Accounting Standards Board
IYC	International Year of Cooperatives
PBIs	Public Benefit Institutions
PSM	Public Service Mutual
MEIs	Mutual Equity Interests
NDIS	National Disability Insurance Scheme
NRMA	National Roads and Motorists' Association
TPP	Trans-Pacific Partnership
UWA	University of Western Australia



# **Recommendations**

## **Recommendation 1**

**2.32** The committee recommends that the Commonwealth Government ensures that a national collection of statistics and data is undertaken to provide an accurate picture of the scale and extent of the co-operative and mutual sector.

## **Recommendation 2**

**3.28** The committee recommends that co-operative and mutuals sector be better represented in government policy discussions, and is actively promoted as a possible option for service delivery particularly where community based initiatives are being considered.

## **Recommendation 3**

**3.29** The committee recommends the Commonwealth Government work with states and territories to develop a program of supports to encourage the establishment of new co-operatives and mutual enterprises.

## **Recommendation 4**

**3.49** The committee recommends that a mutual enterprise is explicitly defined in the Corporations Act 2001, and its associated regulations.

## **Recommendation 5**

**3.51** The committee recommends that the role of directors in mutual enterprises is defined in the Corporations Regulations to align with the proposed definition of a mutual enterprise in the Corporations Act.

## **Recommendation 6**

**3.75** The committee recommends the Commonwealth Government work with states and territories to ensure the continual improvement to advice, guidance and information provided at all stages in the establishment, governance and regulation of co-operatives.

## **Recommendation 7**

**3.80** The committee recommends that the Commonwealth Government to work with all relevant stakeholders to undertake a program of education and training to inform them about the role of co-operatives and mutuals.

## **Recommendation 8**

**3.81** The committee recommends that the Commonwealth Government examine ways in which it can improve the recognition and understanding of the co-operative and mutual sector in the national secondary school curriculum and that tertiary institutions consider the inclusion of co-operative and mutuals in accounting, business, commerce, economics and law degrees.

## **Recommendation 9**

**3.82** The Committee recommends that professional accreditation bodies, such as the Law Society and Institute of Chartered Accountants, require a demonstrated knowledge of the co-operatives and mutual structure before it will licence its members to practice accounting or law.

## **Recommendation 10**

**3.92** The committee recommends that the Commonwealth Government amend the Indigenous Advancement Strategy to allow registered co-operatives the same access to allow levels of grant funding as other entities.

## **Recommendation 11**

**3.93** The committee recommends that the Commonwealth Government review, and where necessary amend the eligibility criteria for grants and funds across all of government grants and program guidelines to ensure that co-operatives and mutual enterprises are not excluded on the basis of their business structure.

## **Recommendation 12**

**4.17** The committee recommends that the co-operative and mutual sector be considered when the government is preparing a Regulatory Impact Statement that accompanies new regulatory policies.

## **Recommendation 13**

**4.18** The committee recommends that the Commonwealth Government liaise with its state and territory counterparts to ensure that the regulatory burden for small and medium sized co-operative and mutual enterprise aligns with the needs of these organisations and ensures they are not disadvantaged relative to companies of a similar size.

#### **Recommendation 14**

**4.26** The committee recommends that the Commonwealth Government closely monitor the progress of the International Accounting Standards Board in developing solutions to bring co-operative shares under the definition of capital under AASB 132, and, where possible, facilitate equivalent amendments as expeditiously as possible.

#### **Recommendation 15**

**4.42** The committee recommends that Commonwealth and State Governments support the formalisation of some of innovative market-based approaches to raising capital for small and medium sized co-operative and mutual enterprises, in the form of advice and information, as they become available.

#### **Recommendation 16**

**4.45** The committee recommends that APRA set a target date for the outcome of discussions with the co-operative and mutuals sector on issues of capital raising and bring those discussions to a timely conclusion.

#### **Recommendation 17**

**4.49** The committee recommends that the Commonwealth Government examine proposals to amend the Corporations Act 2001 to provide co-operative and mutual enterprises with a mechanism to enable them access to a broader range of capital raising and investment opportunities.



# **Chapter 1**

## **Introduction**

1.1 On 2 March 2015, the Senate referred the following matters to the Economics Reference Committee for inquiry and report by 14 May 2015.

- (a) the role, importance, and overall performance of cooperative, mutual and member-owned firms in the Australian economy;
- (b) the operations of cooperatives and mutuals in the Australian economy, with particular reference to:
  - (i) economic contribution,
  - (ii) current barriers to innovation, growth, and free competition,
  - (iii) the impact of current regulations, and
  - (iv) comparisons between mutual ownership and private sale of publicly held assets and services; and
- (c) any related matters.

1.2 On 24 March 2015, the Senate granted an extension to the committee to report by 30 November 2015. On 7 September 2015, the Senate granted the committee a further extension to report by 26 February 2016. On 30 November 2015, the Senate granted the committee a further extension to report by 17 March 2016.

### **Conduct of the inquiry**

1.3 The committee received 60 submissions, as listed in Appendix 1.

1.4 The committee held three public hearings in Sydney, Melbourne and Canberra. The witnesses are listed in Appendix 2.

### **Structure of the report**

1.5 The report addresses the committee's terms of reference and is divided into four chapters:

- Chapter one (this chapter) states the administrative arrangements for the inquiry;
- Chapter two defines the concepts and issues discussed in the report;
- Chapter three discusses the broad issues facing the cooperative and mutuals sector, examines the perceived recognition and establishment barriers faced by organisations in the sector; and
- Chapter four concludes the report and considers regulation and access to capital.

**Term of reference (b)(iv) - Comparisons between mutual ownership and private sale of publicly held assets and services**

1.6 The inquiry's terms of reference ask the committee to compare mutual ownership of publicly held assets to the private sale of those assets. During the course of the inquiry, the committee did not receive enough evidence on this issue that would allow it to undertake a comparative analysis of the preferred model for management of publicly held assets. However, the committee did receive submissions from BCCM and a small number of other mutual enterprises recommending the Public Service Mutual (PSM) model as a possible vehicle for the delivery of public services. The Community and Public Sector Union (CPSU) argued against the prospect referring to experiences in the United Kingdom.

1.7 As such, while the report does consider opportunities for co-operative and mutual enterprises, and some of these will be in areas that could be considered traditional public services, it does not address this term of reference.

**Notes on references**

1.8 References to submissions in this report are to individual submissions received by the committee and published on the committee's website. References to the committee Hansards are to the official transcripts from inquiry hearings.

**Acknowledgements**

1.9 The committee thanks the many individuals and organisations that made written submissions, as well as those who gave evidence at the public hearings.



## Chapter 2

### Cooperatives, mutuals and member-owned firms

2.1 The committee received evidence during the inquiry which used the terms co-operative, mutual or member-owned firm interchangeably. The approach taken in this report is informed by the Business Council of Co-operatives and Mutuals (BCCM), who describe their member organisations as Co-operative Mutual Enterprises (CMEs). The statement by Mr Graeme Nuttall, who in 2012 reviewed employee ownership in the UK for the Department for Business, Innovation and Skills, probably put it more succinctly by stating that, '*All co-operatives are mutuals, but not all mutuals are co-operatives*'.<sup>1</sup> The committee would add...*but both are member-owned firms*.

2.2 As the peak representative body for CMEs in Australia, the BCCM contends that:

...CMEs are not well understood in markets or by regulators in Australia. They are formed to pursue different purposes from investor-owned companies but they exist and compete in the same markets as those entities. A greater understanding of their purpose and their governance model will provide a basis for the development of policies that enable Australia to obtain the best value from this business model.<sup>2</sup>

2.3 Contextually, BCCM sees CMEs contributing widely to the Australian economy.

...They distribute wealth, control and ownership...they are self-help organisations that bring diversity, competitive forces and consumer choice to markets. They address market failure by enabling smaller market participants, enterprises or individuals, to compete in markets that favour larger entrants. Finally, they present an alternative public service delivery model for government that combines commercial focus, community ownership and a commitment to the pursuit of the social purpose. The submission will provide a comparison between the privatisation and the mutualisation of government services and assets.<sup>3</sup>

2.4 The BCCM doesn't distinguish the two business models, rather it combines the two types of enterprise and differentiates them only in terms of the regulatory environment they operate in, and their contrast with other business models:

CMEs include both not for profit and for profit entities. They run lean and efficient business operations for their members and their

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1 UK Government, *Sharing Success: The Nuttall Review of Employee Ownership*, November 2012, Annexe A – Background to the Review, p. 74.

2 Business Council of Co-operatives and Mutuals, Submission No 3, p. 2.

3 Business Council of Co-operatives and Mutuals, *Submission No 3*, p. 2.

communities...There are regulatory differences: co-operatives are incorporated and regulated under state and territory laws, mutuals are regulated under the federal Corporations Act.

Despite regulatory differences, CMEs share important characteristics that distinguish them from companies. They are a self-help response to the mutually identified needs of individuals or organisations. They are driven to meet both financial and social goals.<sup>4</sup>

**Table 1.1 – Types of cooperatives and mutuals**

Type	Description	Examples
Consumer owned	<ul style="list-style-type: none"> <li>Members jointly purchase programs and services, improving value for money and access to expert advice.</li> <li>Formed by members to increase their bargaining power in the market (e.g. bulk buying from suppliers to gain volume discounts).</li> </ul>	<ul style="list-style-type: none"> <li>Consumer retail societies: The Barossa Community Store Co-op</li> <li>Collective purchasing cooperatives: The Co-op (University Bookshop) (also see consortium enterprises)</li> <li>Customer owned banks and credit unions: Teachers Mutual Bank, bankmecu</li> <li>Motoring clubs: NRMA, RAC WA</li> <li>Health mutuals and non-profit health insurers:</li> </ul>
Employee owned	<ul style="list-style-type: none"> <li>Provide members with an income as well as empower employees with a stake in the organisation's decision-making process.</li> <li>Pursue long-term strategies that smooth out the peaks and troughs of the business cycle.</li> </ul>	<ul style="list-style-type: none"> <li>Employee benefits trust cooperatives: Sunderland Homecare Cooperative</li> <li>Worker cooperatives: Cooperative Home Care, Nundah Community Enterprise Cooperative</li> <li>Not all employee-owned businesses are cooperatives (for example, accounting and legal firms are limited liability partnerships).</li> </ul>
Enterprise owned	<ul style="list-style-type: none"> <li>Enable self-employed members and member businesses or community groups to band together and find strength in numbers.</li> <li>Includes secondary cooperatives, a consortium cooperative where all members are cooperatives and consortium mutuals which umbrella organisations with like needs.</li> </ul>	<ul style="list-style-type: none"> <li>Consortium cooperatives: Community Child Care Cooperative</li> <li>Community cooperatives: Dandenong and District Aboriginal Cooperative</li> <li>Agricultural cooperatives: Murray Goulburn, CBH Group; Coleambally Irrigation Cooperative Limited</li> <li>Market trader cooperatives: Capricorn Society, Hunternet</li> <li>Artisan cooperatives: Associated Newsagents Cooperative SA, Hairdressers' Cooperative</li> </ul>
Hybrid – multi-stakeholder	<ul style="list-style-type: none"> <li>Hybrid cooperatives combine any elements of the three other types of cooperatives.</li> </ul>	<ul style="list-style-type: none"> <li>Housing cooperatives: Common Equity Housing Ltd – a consumer and enterprise cooperative</li> </ul>

2.5 Table 1.1 (above), produced by Ernst and Young (EY) describes the typical types of CMEs currently operating in Australia, and provides examples of each type.

2.6 In their submission, EY submitted that the difference between co-operatives and mutuals is historical, except for the fact that co-operatives have to subscribe to the seven principles of the International Co-operative Alliance (*see para 2.10*). Their submission added that historically the term mutuals referred to 'member-owned businesses in banking, superannuation and healthcare.'<sup>5</sup>

## Definitions

2.7 The following definitional sections provide descriptions of the types of co-operatives and mutuals that fall under these business models.

### *Co-operatives*

2.8 The defining characteristic of a co-operative is that it is owned by their members and acts in the interests of their members, rather than to provide benefit to shareholders or investors. Two types of cooperatives are provided for under current Australian law: Distributive and Non-Distributive.

2.9 A Distributive Co-operative, commonly known as a Trading Co-operative, is typically a commercial enterprise where members may share the financial surplus. Whereas a Non-Distributive Co-operative uses any surplus to 'further the activities of the co-operative'.<sup>6</sup>

2.10 Co-operative Development Services Ltd provides a list on their website of further characteristics that both types of co-operative typically have. A trading co-operative is characterised by the following:

- A member must support an activity associated with the primary activity of the co-operative, e.g. a dairy farmer is required to deliver an agreed quantity of milk to the co-operative in any given period to remain an 'active' member.
- A trading co-operative must have a share capital.
- Disclosure statements are required for formation and issuing shares.
- Bonus shares can be issued to members upon asset sale or revaluation.
- Shares can be issued at a premium.
- Members may be required to subscribe to more shares or lend money to the co-operative.
- Surplus funds can be distributed to members by way of a 'limited' dividend on shares held, bonus shares and/or a rebate in proportion to the business done by the member with the co-operative.

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5 Ernst & Young, *Submission 44*, p. 9.

6 Mercury Centre Cooperative Ltd, *Submission No 43*, p. 5.

- Surplus funds from winding up is distributed to members in proportion to share capital held by a member.

2.11 A trading co-operative or distributive co-operative, can provide a pecuniary benefit to members, and as such, is subject to a disclosure regime under Australian co-operatives legislation. A non-trading co-operative is not subject to the disclosure regime. Surplus funds from winding up are distributed to another similar 'not-for-profit' organisation approved by members of the co-operative.

2.12 A non-trading co-operative has the following features:

- A member must maintain a relationship with the co-operative associated with its primary activity, e.g. a parent must have a child enrolled in a child care co-operative to be an 'active' member. Payment of a regular subscription by a member is also sufficient to establish 'active' membership of a non trading co-operative.
- No disclosure statement required for formation (except NSW) or issuing shares.
- Shares cannot be issued at a premium.
- Bonus shares cannot be issued either from asset revaluation or sale, or from profits.
- Members cannot be compelled to acquire more shares or lend money to the co-operative.
- Profits made from trading are reinvested in the co-operative and/or distributed to a charitable organisation.<sup>7</sup>

2.13 To mark the UN International Year of Co-operatives in 2012, the Australian Bureau of Statistics published an article setting out the typical characteristics and activities. The article described how both the distributive and non-distributive co-operatives would 'require their members to maintain an active relationship with the co-operative'....and this can 'include purchasing or supplying goods or services, paying an annual subscription, or being a tenant of a housing co-operative.' The article also described the range of activities that are often undertaken by co-operatives in Australia:

[C]onsumer (buying and selling goods to members at a competitive rate); marketing (branding, marketing and distributing members' products and services); service (providing services to members, such as health, electricity or housing); and community (resource, information and skill sharing that encourages ownership and participation). Financial co-operatives comprise credit unions, mutual building societies and friendly societies.<sup>8</sup>

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7 Co-operative Development Services Ltd, *Australian legal structures*, available at: <http://www.coopdevelopment.org.au/typesofcoops.html>, (accessed 25 February 2016).

8 Australian Bureau of Statistics, *Co-operatives in Australia – An Overview*, Available at: <http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/by%20Subject/1301.0~2012~Main%20Features~Co-operatives%20in%20Australia%20-%20an%20overview~285>, (accessed on 22 February 2016).

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### *Australian tax law*

2.14 Co-operative companies are defined in Australian tax legislation as a company that has certain limitations on its shareholding and trading, and that has one, or all, of the following as its object:

- (a) the acquisition of commodities or animals for disposal or distribution among its shareholders;
- (b) the acquisition of commodities or animals from its shareholders for disposal or distribution;
- (c) the storage, marketing, packing or processing of commodities of its shareholders;
- (d) the rendering of services to its shareholders;
- (e) the obtaining of funds from its shareholders for the purpose of making loans to its shareholders to enable them to acquire land or buildings to be used for the purpose of residence or of residence and business.<sup>9</sup>

### *International Co-operative Alliance principles*

2.15 The International Co-operative Alliance sets out a list of principles that guide how co-operatives should operate, and that distinguish them from other forms of enterprise:

#### **1. Voluntary and Open Membership**

Co-operatives are voluntary organisations, 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.

#### **2. Democratic Member Control**

Co-operatives are democratic organisations 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 co-operatives members have equal voting rights (one member, one vote) and co-operatives at other levels are also organised in a democratic manner.

#### **3. Member Economic Participation**

Members contribute equitably to, and democratically control, the capital of their co-operative. At least part of that capital is usually the common property of the co-operative. 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 co-operative, possibly by setting up reserves, part of which at least would be indivisible; benefiting members in proportion to their transactions with the co-operative; and supporting other activities approved by the membership.

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9 *Income Tax Assessment Act 1936*, ss. 117(1).

#### **4. Autonomy and Independence**

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

#### **5. Education, Training and Information**

Co-operatives provide education and training for their members, elected representatives, managers, and employees so they can contribute effectively to the development of their co-operatives. They inform the general public - particularly young people and opinion leaders - about the nature and benefits of co-operation.

#### **6. Co-operation among Co-operatives**

Co-operatives serve their members most effectively and strengthen the co-operative movement by working together through local, national, regional and international structures.

#### **7. Concern for Community**

Co-operatives work for the sustainable development of their communities through policies approved by their members.<sup>10</sup>

### ***Mutuals***

2.16 Similarly, the distinguishing characteristic of a mutual organisation is that it 'is owned by its members, and run exclusively for their benefit, rather than for the benefit of outside investors'.<sup>11</sup>

2.17 Internationally, mutuals tend to be larger organisations than co-operatives, and specialise in specific business sectors. In Canada mutuals are often insurance companies where the policy holder is a participant in the business.<sup>12</sup> According to Co-operatives and Mutuals Canada this results in a 'very stable and successful business model'.<sup>13</sup>

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10 International Co-operative Alliance, *Co-operative identity, values and principles*, available at: <http://ica.coop/en/whats-co-op/co-operative-identity-values-principles>, (accessed 1 March 2016).

11 UK Government, Department for Business Innovation & Skills, *A guide to Mutual Ownership Models*, November 2011, p. 2.

12 Co-operatives and Mutuals Canada, *Co-operatives and Mutuals, What is a Mutual?*, available at: <http://www.canada.coop/en/co-operatives-and-mutuals/what-co-op-what-mutual>, (accessed on 23 February 2016).

13 Co-operatives and Mutuals Canada, *Co-operatives and Mutuals, What is a Mutual?*, available at: <http://www.canada.coop/en/co-operatives-and-mutuals/what-co-op-what-mutual>, (accessed on 23 February 2016).

2.18 In the UK the Communities and Local Government Committee used the definition of a mutual from Mutuo who described mutuals in similar terms to co-operatives:

...organisations which are owned by, and run for the benefit of their current and future members. These are different to social enterprises in that a large proportion of the business should be owned by either employees and/or the local community.

2.19 However the UK committee's report also pointed out the differences between the two concepts, differentiating them on the basis that co-operatives subscribe to the following principles of the International Co-operative Alliance:

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...<sup>14</sup>

2.20 The advantages of the mutual model in comparison to other business structures was highlighted by Regis Mutual Management set out what it sees as the economic benefits unique to mutual enterprises:

**Cost effectiveness** – Mutuals deliver better value, broader and more appropriate insurance protection for members as well as a reduction in overhead costs.

**Increased Competition** – Mutuals drive competition and diversity into the market. This is particularly important in the financial services sector.

**Supporting Australian Financial Services Sector** - Insurance or reinsurance business that might otherwise be ceded to foreign markets can be retained within the domestic market.

**Creating Jobs** - The use of mutual structures has the potential to create greater domestic employment in areas which benefit the community.<sup>15</sup>

## The scale and extent of the sector

2.21 The scale of CMEs in Australia and internationally is significant. The UN's International Year of Cooperatives (IYC) was launched in recognition of the scale of the sector, citing the International Cooperative Alliance's membership of 800 million alone.<sup>16</sup>

2.22 The UN IYC was also promoted on the basis that cooperatives have the ability to extend far beyond the reach of other businesses in areas such as job creation, social inclusion and achieving positive environmental outcomes:

Cooperatives represent a model of economic enterprise, which when effectively implemented, promotes democratic and human values as well as

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14 UK Parliament, House of Commons, Communities and Local Government Committee, *Mutual and co-operative approaches to delivering local services*, 2012, Chapter 2, para 10.

15 Regis Mutual Management, *Submission 33*, p. 5.

16 United Nations, International Year of Cooperatives, Launch Programme, p. 3. Available at: <http://social.un.org/coopsyear/documents/launchprogramme.pdf>, (accessed 23 February 2016).

respect for the environment...Cooperatives help create, improve and protect income as well as they generate employment opportunities and contribute to poverty reduction. As of 2007, cooperatives were responsible for more than 100 million jobs worldwide. Cooperatives also promote social integration and cohesion as they are a means of empowering the poor and marginalized groups. As such, they also play an ever-increasing role in the promotion of gender equality and the social and economic empowerment of women.<sup>17</sup>

2.23 In Australia the Australia Institute estimates that eight in ten Australians are members of some form of CME, but tellingly, only a fraction of that number actually realise it.<sup>18</sup>

2.24 The Australia Institute also estimated the size of the sector in Australia and worldwide, the economic and social impact it has through the creation of jobs, and the types of industries where cooperatives and mutuals thrive:

**Table 1.2: Overview of member owned businesses**

Worldwide	Australia
1,000 million members	13.5 million members (estimated)
\$1,700 billion annual turnover	1,600 co-operatives
100 million employed	103 financial mutuals
Three billion livelihoods secured	\$83 billion combined total assets of financial mutuals
23% share of global insurance market	\$17 billion: top 100 turnover in 2011
196 million credit union members	Seven million automobile club members

Source: Cooperatives UK (2011); The UK co-operative economy 2011 – Britain's return to co-operation; World Council of Credit Unions; ABS (2012); socialbusiness.coop, Cooperatives Australia (2012).

### **Measuring CMEs**

2.25 A key element in measuring the economic and social impact of the work of CMEs is the collection of data that illustrates the work of CMEs across a variety of sectors, as well as the effect the Co-operatives National Law (CNL) is having on the sector.

2.26 Robyn Donnelly, a former employee of the NSW Registry of Co-operatives who was on the intergovernmental committee that developed the CNL, submitted that the paucity of data on the breadth of activity by CMEs is preventing a full picture of

17 United Nations, International Year of Cooperatives, Launch Programme, p. 3. Available at: <http://social.un.org/coopsyear/documents/launchprogramme.pdf>, (accessed 23 February 2016).

18 The Australia Institute, *Who knew Australians were so co-operative? The size and scope of mutually owned co-ops in Australia*, 2012, Institute Paper 10, available at: [http://www.tai.org.au/sites/default/files/IP%2010%20Who%20knew%20Australians%20were%20so%20co-operative\\_4.pdf](http://www.tai.org.au/sites/default/files/IP%2010%20Who%20knew%20Australians%20were%20so%20co-operative_4.pdf), (accessed 22 February 2016).



the sector being developed, and thus hindering the development of appropriate policies to address the issues facing the sector:

The development of good policy requires information. There is no national database for co-operatives. State Registrars do not generally publish statistics about the number of co-operatives in their jurisdictions or the number of co-operatives that transfer incorporation or that are deregistered. Unlike the monthly publication of statistics by companies there is very little information to test the impact of any regulation for co-operatives.<sup>19</sup>

2.27 The Mercury Centre in Sydney contended that the lack of data and subsequent understanding of co-operative and mutual enterprises (CMEs) in key government agencies is systemic and detrimental:

The BCCM summary identified that the key barriers are those areas of recognition, education and regulation. The Mercury Centre concurs with this assessment, particularly in the context of government regulation,...However, the Mercury Centre considers that further important issues include (1) structural efficiency and organisational capacity, (2) measurement and impact and (3) community and public asset ownership.<sup>20</sup>

2.28 To help alleviate this lack of data around the sector, BCCM commissioned the University of Western Australia's Co-operative Enterprise Research Unit (CERU) to undertake a study into the top 100 CMEs in Australia. Dovetailing with this work is the continued development of the Australian Co-operative and Mutual Business Index (ACMI) that commenced in 2012, also being undertaken by the Co-operative Enterprise Research Unit (CERU) within the University of Western Australia (UWA) Business School. The research is designed to map the size and structure of the sector, to provide a 'better understanding of these Australian Co-operative and Mutual businesses and their contribution to the national economy.'<sup>21</sup>

2.29 The initial findings estimated the combined turnover of these enterprises was approximately \$25 billion, while their combined assets amounted to \$108 billion.<sup>22</sup> The pie chart (Figure 1) below illustrates the diversity of the sector, with CMEs active in a number of key industries.

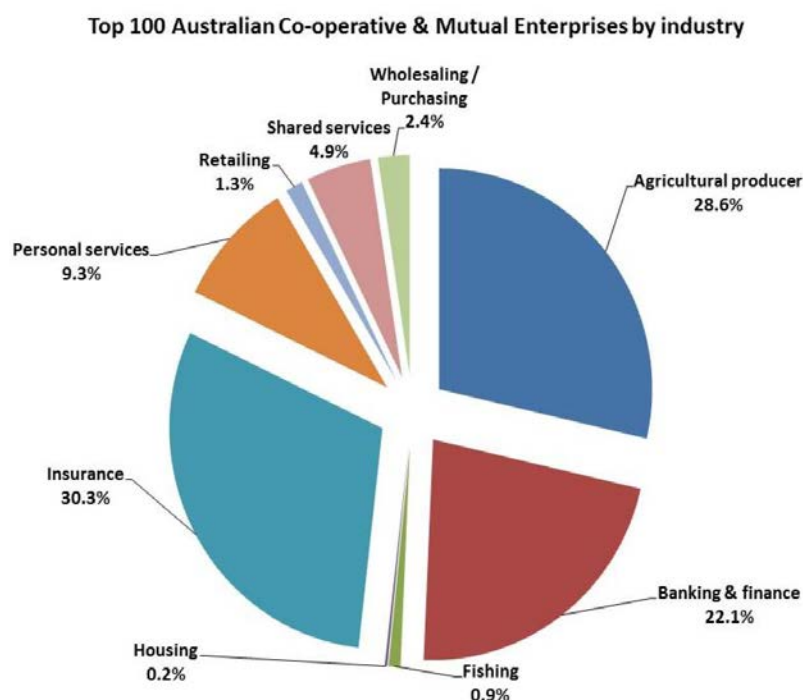
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19 Ms Robyn Donnelly, *Submission 57*, p. 5.

20 Mr Peter Tregilgas, Mercury Centre Co-operative Ltd., *Committee Hansard*, 29 October 2015, p. 57.

21 Centre for Entrepreneurial Management and Innovation, *Australia's Leading Co-operative and Mutual Enterprises in 2014*, p. 5. Available at: [http://www.cemi.com.au/sites/all/publications/CEMI\\_DP1403-Mazzarol-Limnios-Soutar-Kresling-2014.pdf](http://www.cemi.com.au/sites/all/publications/CEMI_DP1403-Mazzarol-Limnios-Soutar-Kresling-2014.pdf), (accessed 1 March 2016).

22 The Conversation, *Australia's co-operative and mutual enterprises deserve greater recognition*, available at: <http://theconversation.com/australias-co-operative-and-mutual-enterprises-deserve-greater-recognition-34284>, (accessed 1 March 2016).

**Figure 1**

Australia's Top 100 CME by industry sector T. Mazzarol (2014)

2.30 A breakdown of these figures by industry and overall value, including earnings and net profit after tax is set out in Table 1.3 below:

**Table 1.3 Top 100 Australian Co-operative and Mutual Enterprises<sup>23</sup>**

Sector	Number	Combined Turnover (\$m)	Median Turnover (\$m)	Median EBIT (\$m)	Median NPAT (\$m)	Combined Assets (\$m)
Agricultural sector	13	7 217.2	210.0	0.4	0.8	4 376 700
Banking and Finance	38	5 570.9	78.5	7.1	4.6	84 476 700
Fishing	2	228.8	114.4	1.7	1.3	66 700
Housing	1	41.2	41.2	1.8	1.8	683 800
Insurance	25	7 638.8	106.4	9.0	9.0	10 781 100
Personal Services	6	2 336.6	477.6	38.8	36.2	7 003 300
Retailing	7	335.9	28.7	0.4	0.3	168 500
Shared Services	2	1 237.8	618.9	9.8	7.1	110 500
Wholesale/Purchasing	6	601.6	83.3	0.6	0.4	186 100
<b>Total</b>	<b>100</b>	<b>25 208.8</b>				<b>107 853 000</b>

Notes to table: EBIT = earnings before interest and tax; NPAT = net profit after tax.

2.31 To supplement this research BCCM recommended that data should be collected at a state and territory level and then collated at a federal level. An initial

23 Centre for Entrepreneurial Management and Innovation, *Australia's Leading Co-operative and Mutual Enterprises in 2014*, p. 5. Available at: [http://www.cemi.com.au/sites/all/publications/CEMI\\_DP1403-Mazzarol-Limnios-Soutar-Kresling-2014.pdf](http://www.cemi.com.au/sites/all/publications/CEMI_DP1403-Mazzarol-Limnios-Soutar-Kresling-2014.pdf), (accessed 1 March 2016).

first step in this process should be for the ABS to begin regular collecting/disaggregating and reporting on relevant data across the CME sector.<sup>24</sup>

## **Recommendation 1**

**2.32 The committee recommends that the Commonwealth Government ensures that a national collection of statistics and data is undertaken to provide an accurate picture of the scale and extent of the co-operative and mutual sector.**

### *The diversity of co-operatives*

2.33 As illustrated at Figure 1 above, CMEs operate in almost every sector of the economy. The committee received evidence from a cross section of these organisations.

2.34 The Voluntary Parents Services Co-operative appeared before the committee in Sydney and explained how they provided a service which brought parents together in fundraising efforts for schools across NSW. The co-operative has reportedly raised \$100 million.<sup>25</sup>

2.35 Also in the education field, Australia Scholarships Group (ASG) is a co-operative of parents established more than 40 years ago to assist them to plan for the children's education. As the largest member-owned education services provider in Australia and New Zealand, ASG provides a range of education plans across public, independent and private school systems, to more than 155 000 members.<sup>26</sup>

2.36 Supporting the tertiary education sector is the Co-op Book Shop, an institution across Australian university campuses. It operates in half of Australia's universities with 60 book shops and is Australia's largest co-operative with nearly two million members.<sup>27</sup>

2.37 Yenda Producers Co-operative are a growers' co-operative of around 1550 producers in the Riverina region of New South Wales. The committee heard that while they have similar goals to other business entities in that they have to make a profit, the impact of their activities in the local community goes well beyond that:

In the local area, we employ 80-odd local people and their families who contribute to our local community. The wages bill is around \$4½ million in the year just gone. As well as that, we support over 100 local charities and schools—you name it; if someone puts their hand up, generally we are there to support them in the local area. We are a distributing co-op, so we do pay rebates and dividends back to our shareholders. In the last five years, those dividends and rebates have amounted to over \$7 million back into the local community.<sup>28</sup>

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24 Business Council of Cooperatives and Mutuals, *Submission 3*, p. 7.

25 Voluntary Parents Services Co-operative, *Committee Hansard*, 29 October 2016, p. 1.

26 Australian Scholarships Group, *Committee Hansard*, 30 October 2016, p. 52.

27 The Co-op, *Submission 38*, p. 2.

28 Yenda Producers Co-operative, *Committee Hansard*, 29 October 2016, p. 24.

2.38 A very different co-operative of bus operators in Victoria also provided evidence to the committee. The Bus Association Victoria (BusVic) is a member-owned, voluntary professional association for Victoria's private, accredited bus and coach operators. The co-operative represents its members in a variety of ways including advocacy with respect to their relations with government, which includes contract negotiations and legislative and regulatory compliance issues.<sup>29</sup>

2.39 The Central New South Wales Renewable Energy Co-operative Ltd (CENREC) and the Community Power Agency Co-operative Ltd are two organisations in the growing co-operative energy sector. CENREC was formed by a number of community members in Bathurst and Orange to invest in a proposed project by Infigen Energy to develop a windfarm at Flyers Creek.<sup>30</sup> Community Power Agency Co-operative Ltd provides support some of the 60 community energy projects around Australia.<sup>31</sup>

2.40 Another organisation established to assist and support other co-operatives and social enterprises, is the Mercury Centre Co-operative. The Mercury Centre advises business on how to establish and develop social enterprise business models through collaboration and shared resources built on community and ethical values.<sup>32</sup>

2.41 The community and social housing sector also features many co-operative organisations. SouthEast Housing Co-operative Ltd. in Victoria told the committee that while the sector is relatively small in Australia to date, internationally it is the preferred model for the provision and maintenance of social housing.<sup>33</sup>

2.42 In response to community concerns around the lack of affordable GPs and healthcare, the National Health Co-operative was established in 2006 in the West Belconnen community of North Canberra. The co-op is now open at six locations in Northern Canberra. These clinics are fully accredited to the RACGP 4th Edition Standards and Charnwood is also accredited as a GP Registrar training practice. Regular clinics are also conducted at six nursing homes closely located to the practice sites. Members have access to bulk-billed GPs and allied health visits (subject to MBS guidelines and regulations), and 30,000 people have now registered as patients.<sup>34</sup>

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29 Bus Association Victoria, *Submission 5*, p. 5.

30 Central New South Wales Renewable Energy Co-operative Ltd, *Committee Hansard*, 29 October 2016, p. 42.

31 Community Power Agency Co-operative Ltd., *Committee Hansard*, 29 October 2016, p. 43.

32 Mercury Centre Co-operative, *Submission 43*, p. 8

33 SouthEast Housing Co-operative Ltd., *Committee Hansard*, 30 October 2016, p. 46.

34 National Health Co-operative, *Welcome*, available at: <http://www.nhc.coop/>, (accessed 2 March 2016).

## **Mutuals**

2.43 Many of the largest mutuals provided evidence to the committee. The Customer Owned Banking Association (COBA) is the peak body for Australia's credit unions, building societies and mutual banks. The sector represented by COBA are collectively the largest holder of household deposits outside the four major banks.<sup>35</sup>

2.44 The National Roads and Motorists' Association (NRMA) are another one of Australia's most well-known and largest mutuals with 2.4 million members in NSW and the ACT. They, along with other motorists' organisations and car clubs under the banner of the Australia Automobile Association, have seven million members. The NRMA is a for-profit organisation.<sup>36</sup>

2.45 Australian Unity is a large mutual organisation that has been operating for 175 years, and provides health care, aged care and financial services to around 850 000 people. Again, it is run on a for-profit basis, but as with all mutuals, these profits are re-invested in the organisation for the benefit of its members.

2.46 Another area where mutuals have a strong presence is the insurance industry. Hirmaa appeared before the committee representing 18 health insurance organisations. These organisations collectively provide insurance to around one million people, and comprise a variety of the business structures, with mutuals or member-owned insurers being the most prevalent.

2.47 Superannuation is also a field where the mutual structure is heavily favoured. Industry Super appeared before the committee and set out the scale of their operations. From relatively small beginnings where the industry funds had 200 000 members and managed \$2.5 million in assets, they now have a membership of nearly five million and hold assets of around 376 billion.<sup>37</sup>

## **Current state and federal legislation governing co-operatives and mutuals**

2.48 The development of the Co-operatives National Law (CNL) began in 2012 through the Council of Australian Governments (COAG). The intention was that each state and territory would pass uniform legislation or legislation consistent with the CNL by May 2014.<sup>38</sup>

2.49 New South Wales are the lead jurisdiction for the legislation which is intended to reduce red tape and subsequent business costs involved in registering and governing a co-operative across jurisdictions. To date NSW, Victoria, Tasmania,

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35 Customer Owned Banking Association, *Committee Hansard*, 29 October 2016, p. 47.

36 National Roads and Motorists' Association, *Committee Hansard*, 29 October 2016, p. 53.

37 Industry Super Australia, *Committee Hansard*, 30 October 2016, p. 25.

38 Tasmanian Consumer Affairs and Fair Trading, *Co-operatives National Law – A Tasmanian Perspective*, p. 1. Available at: [http://www.consumer.tas.gov.au/data/assets/pdf\\_file/0007/247930/Summary\\_of\\_national\\_approach\\_-\\_Tasmanian\\_perspective.pdf](http://www.consumer.tas.gov.au/data/assets/pdf_file/0007/247930/Summary_of_national_approach_-_Tasmanian_perspective.pdf), (accessed 29 February 2016).

South Australia and the Northern Territory have adopted the legislation.<sup>39,40</sup> WA has amended its *Co-operatives Act 2009* (WA Act) to align with the CNL.

2.50 Nevertheless, some inconsistencies remain. While Queensland has withdrawn from the agreement altogether, there are indications that it may yet amend its existing legislation to be consistent with the national law. ACT is planning the introduction of its enabling laws in 2017.<sup>41</sup>

2.51 There are four elements to the legislation, the enabling Act, the Co-operatives National Law, the Co-operatives National Regulations and the local regulations. All jurisdictions that adopt the law will have these elements.

2.52 The NSW government provided information to the committee explaining the objects of the CNL, and the expected outcomes. One of the overriding objectives is to 'ensure that there are no competitive advantages or disadvantages for co-operatives as compared to corporations'.<sup>42</sup> The main reforms to achieve this are:

- Improved consistency of co-operatives legislation through the introduction of uniform template laws with the option to use alternative consistent legislation;
- Cross border business reform, with automatic authorisation arrangements replacing the requirement for a co-operative to register in each State or Territory in which it wants to do business;
- Simplification of financial reporting and audit requirements for small co-operatives;
- More flexible options to raise funds from members or external sources through the introduction of co-operative capital units (CCUs) in all jurisdictions;
- Responsibilities and duties of directors and officers of a co-operative updated and made consistent with the *Corporations Act 2001 (Cth)* (the Act);
- Improved consistency and referencing of the Act where it can be appropriately applied to co-operatives, such as certain administration and winding up matters;
- Setting out the responsibilities of the secretary of a co-operative and the consequences of not meeting those responsibilities;

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39 Ms Robyn Donnelly, *Submission 57*, p. 3.

40 Commencement dates for the each state or territory to date are: NSW and Victoria – 3/3/14; SA – 22/05/15; Northern Territory – 1/07/15; Tasmania – 1/09/15.

41 Bright Law, *Co-operatives National Law Update 2016*, available at: <http://www.brightlaw.com.au/corporate-governance/co-operatives-national-law-update-2016/> (accessed 29 February 2016).

42 NSW Fair Trading, *Submission 59*, p. 4.

- Removing the requirement for a formation disclosure statement for a proposed non-distributing co-operative, unless requested to provide this statement by the regulator;
- The naming of the types of co-operatives was changed from 'trading' and 'non- trading' co-operative to 'distributing' and 'non-distributing' co-operative to better reflect the nature of the co-operative;
- Former members' rights have been reduced from 5 years to 2 years duration in line with stakeholder feedback. Schedule 3 (1) of the CNL provides for a savings provision in the CNL Adoption Act of a jurisdiction, to maintain the existing former members' rights under their Co-operatives Act before the commencement of the CNL;
- Capacity for enforceable undertakings between a person and the regulator has been introduced to enable a cost effective means of ensuring compliance by co-operatives with the law;
- In NSW, about half the fees in its CNL Local Regulations have been reduced, when compared with the corresponding fee under the previous NSW Co-operatives Regulation 2005;
- Introduction of a fee for the lodging of annual returns or annual reports by a co- operative, to help to recoup the costs of the NSW Registry Services in reviewing these documents for compliance with the CNL.<sup>43</sup>

2.53 To support transition to the new regulatory environment the states and territories that have enacted the CNL have put in place administrative arrangements to provide information and assistance to those seeking to establish a co-operative, or for established organisations.

2.54 Consumer Affairs and Fair Trading in Tasmania for example has published a number of fact sheets on the CNL as well as documentation on the new fees and registration processes.<sup>44</sup> While Consumer and Business Affairs in South Australia has a new section on its website which includes administrative and governance arrangements as well as information and advice on how to run a co-operative.<sup>45</sup> Chapter 3 includes further discussion of the adequacy of information and advice from state and federal agencies, as well as commentary on the CNL.

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43 NSW Fair Trading, *Submission 59*, p. 5.

44 Government of Tasmania, Consumer Affairs and Fair Trading, *Co-operatives*. Available at: [http://www.consumer.tas.gov.au/forms\\_and\\_fees](http://www.consumer.tas.gov.au/forms_and_fees), (accessed 1 March 2016).

45 Government of South Australia, Consumer and Business Services, *Co-operatives*. Available at: <http://www.cbs.sa.gov.au/licensing-and-registration/co-operatives/>, (accessed 1 March 2016).





## Chapter 3

### The barriers to growth, innovation and competition

3.1 There were a number of issues raised by submitters and witnesses throughout the inquiry. The majority of the issues raised were by relatively large co-operatives, or national mutual organisations and the concerns generally reflected the interests of organisations of that scale.

3.2 The issues raised by submitters relate to the perceived barriers the sector believes are preventing co-operatives and mutuals from forming and realising their full potential.

3.3 This chapter discusses the following barriers in turn: the lack of recognition of co-operatives and mutuals and their contribution to the economy; a lack of information and advice for new and existing co-operatives; concerns around the requirements of establishing a co-operative; and finally, issues unique to Indigenous co-operatives.

#### Recognition of the contribution and potential of co-operatives and mutuals

3.4 Despite the huge numbers of people that belong to a co-operative or a mutual in Australia, submitters argued that there is still limited awareness and recognition of the sector, and the benefits it can bring. According to submitters, co-operatives and mutual enterprises (CMEs) should be given equal footing amongst other business structures, a competitively neutral environment created, and recognition of this scale and the potential benefits of the sector needs to be enhanced.

3.5 The Co-op Book Shop cited a lack of recognition as one of the broad restricting factors that was inhibiting the growth of the sector:

That is the main restriction that we have. As far as the broader issues go, to help cooperatives flourish and grow in the future, it is about having the recognition of what you are bringing to our industry and shining a light on our industry. That is one of the reasons that we formed the Business Council of Co-operatives and Mutuals [BCCM]. Eighty per cent of Australians belong to one; they just do not know it, in the main.<sup>1</sup>

3.6 The International Co-operative Alliance emphasised that globally co-operatives were increasingly being recognised as being a key element in a pluralistic and diverse economy that can contribute in a broader economic sense, as well as delivering for communities and their members:

I think what we are seeing is a global recognition developing about the cooperative difference and the need to ensure that countries have more pluralistic and diversified national economies. There is clear evidence that

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<sup>1</sup> Mr Peter Knock, the Co-op Book Shop, *Committee Hansard*, 29 October 2015, p. 38.

those who did rode through the financial crisis and the recession much better than anyone else.<sup>2</sup>

3.7 The idea that the co-operative model can assist enterprises to be globally competitive was supported by the example of a grain growers co-operative in Western Australia who found that their co-operative model allows them to remain competitive in a global market place by sharing costs and continually re-investing in their supply chain process:

In WA our supply chain is 90 per cent focused on export, and our grain growers are facing international competition in supplying grain into our close Asian markets, so we go to great lengths to keep our growers' supply chain costs to a minimum and reinvest in storage, handling and infrastructure, as well as generating rebates for our growers. So we think our cooperative business model is good for the Australian economy and deserving of recognition and support.<sup>3</sup>

3.8 The Australian Scholarship Group were of the view that despite the contribution that co-operatives and mutuals provided to the economy, they received little support relative to other business sectors:

Cooperatives and mutuals are a key and essential part of the Australian economy, yet they are not accorded the recognition and support that can allow them to play an even bigger role in societal development... there is little or no support of the sector in comparison to the corporate or other business sectors.<sup>4</sup>

3.9 Some submitters argued that the lack of inclusion in high level policy discussions is illustrated by the lack of consideration of co-operatives as one of the bodies that could develop in the modern economy. It was suggested that the government's current legislation around crowd-sourced funding and equity<sup>5</sup> was a policy area where co-operatives, many of which are social enterprises, should have been key to the discussions:

We are seeking recognition of that when the government looks at things like changes to the rules around crowd sourced equity funding. There is a really important discussion taking place in Australia about innovation and adapting to the new world economy that is rising up. That is a brilliant conversation, but I fear that what is potentially missing out of that is the second half of the story, which is social enterprise and social innovation.<sup>6</sup>

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2 Dame Pauline Green, International Co-operative Alliance, *Committee Hansard*, 30 October 2015, p. 10.

3 Dr Andrew Crane, Business Council of Co-operatives and Mutuals, *Committee Hansard*, 30 October 2015, p. 16.

4 Mr John Veleginis, Australian Scholarships Group, *Committee Hansard*, 30 October 2015, p. 52.

5 Corporations Amendment (Crowd-sourced Funding) Bill 2015.

6 Mr Tom Nockolds, Community Power Agency Co-operative Ltd, *Committee Hansard*, 29 October 2015, p. 44.

3.10 The Capricorn Society, the fifth largest CME in Australia with a turnover of \$1.33 billion, contended that government recognition is crucial in developing the sector, and utilising the contribution it can have to the economy:

Co-operatives are the product of addressing the needs of members that market forces currently do not provide for or offer.

Government recognition and support of this core pillar within the Australian economy and landscape through promotion, provision of a developmental framework and an environment of growth are key for CMEs continued and increased contribution to the economy.<sup>7</sup>

### ***Recent Government Reviews that recognised CMEs***

3.11 BCCM acknowledged that recognition of the sector is increasing. They cited a number of recent government reviews and high policy processes that have recognised the contribution the sector can make. These included the Competition Policy Review where the Review Panel noted the potential of CMEs to 'increase diversity in public sector markets, increase consumer choice and control and stimulate public service innovation.'<sup>8</sup>

3.12 The competitiveness of growers' or producers' cooperatives was recognised by the Commonwealth Government in the 2015 Agricultural Competitiveness White Paper. The Paper commits the Commonwealth Government to offering training courses on 'cooperatives and other business structures to help farmers to better engage through the supply chain and attract investment.'<sup>9</sup> In strongly endorsing the advantages of the Co-operative model for farmers, the government also realises that information about the sector needs to be improved:

The benefit of a cooperative structure is it offers family farmers the ability to retain their property ownership but delivers them the scale to better influence what happens beyond the farm gate, and diversify their income. Farmer-owned cooperatives can also add competition in the market place if they add to the number of participants, and allow farmers to engage in additional parts of the value chain where profitable to do so. The recent success of some cooperatives has increased interest in them. But information on how to form a cooperative and the pros and cons of doing so is not readily available. The Government will provide information to help support better decision making on alternative business structures.<sup>10</sup>

3.13 As a consequence of the Agricultural Competitiveness White Paper, the government committed \$13.8 million over two years from 2015-16 for:

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7 The Capricorn Society Limited, *Submission 8*, p. 4.

8 Business Council of Co-operatives and Mutuals, *Submission 3*, p. 14.

9 Australian Government, *Agricultural Competitiveness White Paper, Stronger Farmers Stronger Economy*, 2015, p. 7.

10 Australian Government, *Agricultural Competitiveness White Paper, Stronger Farmers Stronger Economy*, 2015, p. 28.

...a pilot program to improve access for farmers to training and information about co-operatives, collective bargaining and innovative business models. Rural Research and Development Corporations will be funded to develop and deliver the training packages and related materials.<sup>11</sup>

3.14 In terms of social policy the capacity for the co-operative and mutual sector to deliver better social outcomes was also recognised by the McClure Review who recommended that government 'Work with the Business Council of Co-operatives and Mutuals to ensure an enabling regulatory, economic and social environment to support mutuals and co-operatives'.<sup>12</sup>

3.15 However, despite these reviews recognising the valuable role of CMEs, the recent summit in September 2015 of business, community groups and unions called by Prime Minister Turnbull excluded representatives from the CME sector, which BCCM argue represents a backwards step:

Recently, there were national economic reform summits held, and the businesses that represent eight in 10 Australians were not at that table, which would seem to be counterintuitive.<sup>13</sup>

### ***Support to realise the potential of the sector***

3.16 While initial recognition was purported to be a barrier for co-operatives, BCCM explained that even after recognition of the co-operative model is achieved, the next step should be to follow that up with actions that actively assist the sector. Dr Crane argued that the sector deserved not only recognition, but impetus and stimulation equivalent to other sectors in the economy:

A government quite often will embrace the small business sector because it is seen as part of how you energise an economy. It is moving from, 'Okay, we recognise you,' through to, 'Actually, you're something we want to stimulate,' and us being chased with offers of support, 'because the government says this is part of a strong, diverse economy and we want to support it.' So it is moving from recognition into actual proactivity...it is then a sector to be driven and supported.<sup>14</sup>

3.17 The Mercury Centre also submitted that central to the development of co-operatives was the recognition that the model should be included in the definition of social enterprise and represent an ideal governance model for the creation of sustainable businesses. Mercury proposed a number of areas where assistance from government would help realise the potential of co-operatives as social enterprises:

[R]ecognition that the cooperative models for governance of social enterprise may offer greater incentives to sustainable business community

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11 Australian Government, *Mid-Year Economic and Fiscal Outlook 2015-16*, Appendix A, p. 142.

12 Reference Group on Welfare Reform, *A New System for Better Employment and Social Outcomes*, p. 183.

13 BCCM, *Committee Hansard*, 30 October 2015, p. 17.

14 Dr Andrew Crane, Business Council of Co-operatives and Mutuals, *Committee Hansard*, 30 October 2015, p. 16.

trading; an identified need for government assistance for cooperative business services; in measurement, identified need for research on social and economic impact of cooperatives and mutuals; community and public ownership; acknowledgement of cooperatives as a governance model for community participation in government investment and community shares; distributing cooperative model provides a platform to build community investment through community shares or non-transferable withdrawable share capital.<sup>15</sup>

3.18 The introduction and rollout of the National Disability Insurance Scheme (NDIS) was cited as a prime opportunity to showcase CMEs as the type of enterprises that have both a commercial and social element to provide customer focussed and responsive services at community level. However to move into this space, as well as other markets, research and data collection to inform decision makers and promote the sector, are crucial steps:

In the context of the NDIS, there is great opportunity...The submissions attest to the flexibility and innovation of co-ops in a whole range of different market settings. At a policy level, I think people have been blind to this. That is why data, research and making visible what these organisations are doing is so important—not only to themselves but also to policy makers in the first instance, and to advisers and others who can shepherd and help them through this formation phase.<sup>16</sup>

3.19 Like the NDIS, the recent Trans-Pacific Partnership (TPP) trade agreement offers prospects for grower/producer co-operatives to take advantage of the increased opportunities that may become available under the TPP. However according to the Norco dairy co-operative, Australia is not yet taking full advantage of the model due to a lack of education and awareness:

The Free Trade Agreement with China has been a welcome announcement by the Federal Government and will potentially allow Australian processors to compete equally with other dairy exporting countries. However, it seems that many of Australia's trading partners know the value of cooperatives better than Australia...[T]he sector is not well understood in Australia, resulting in little or no educational content at secondary or tertiary levels. It is essential that we educate our young people regarding the benefits and opportunities that the co-operative, mutual and member-owned business model can achieve in Australia.<sup>17</sup>

### ***Benefits of the co-operative model to the agricultural sector***

3.20 The committee received evidence from a number of agribusinesses that promoted the value of the co-operative model to their sector. Professor Cotter made

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15 Mr Peter Tregilgas, Mercury Centre Co-operative Ltd., *Committee Hansard*, 29 October 2015, p. 57.

16 Mr Garry Cronan, Mercury Centre Co-operative Ltd., *Committee Hansard*, 29 October 2015, p. 59.

17 Norco, *Submission 9*, p. 3.

the general point that the disparate and fragmented nature of the sector lent itself to collaborative business models:

Australia's farming and agribusiness systems are fragmented, with few agribusinesses having sufficient capacity to supply high value, high growth export market opportunities on a year-round basis. Collaborative business models are needed to achieve sufficient scale, implement quality assurance processes and co-ordinate activities including product development, marketing and distribution.<sup>18</sup>

3.21 The 'supply and purchasing co-operative' as described by Professor Altman, Dean of Newcastle Business School, is a model which is of particular assistance to small farmers who can replicate the benefits afforded to larger producers by combining their purchasing power:

This type of cooperative is quite important in agriculture where farmers establish a cooperative to obtain goods and services required for their business or for personal use at lower prices than would be possible if they go it alone. Thus farmers can take advantage of economies of scale and scope that are afforded to larger corporate farms.<sup>19</sup>

3.22 Professor Altman also explained the features of a 'marketing co-operative', which is similarly utilised by smaller agribusinesses:

This type of cooperative aligns the interests of producers with regards to marketing output to retailers or wholesalers. A marketing cooperative can also store, process, and package output prior sale. This allows farmers, for example, to take advantage of economies of scale and scope in storage and production, increasing their net income over what it might otherwise be. It also serves to increase the bargaining and marketing power of farmers. In addition, a marketing cooperative can help stabilize farmers' income through its inventory capacity, providing farmers with a relatively stable income as marketing prices fluctuate.<sup>20</sup>

3.23 Co-operative Bulk Handling in Western Australia provided the committee with an example of the co-operative model in action, citing its grain export supply chain:

CBH's integrated business model (storage, handling, transportation, marketing and port operations) seeks to ensure grain growers have greater influence and control throughout each element of the chain, as well as providing the vital interface between growers and their customers.<sup>21</sup>

3.24 Kingfisher Law also emphasised the suitability of the supply and purchasing cooperative model with agribusiness, particularly the irrigation and dairy industries:

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18 Professor Julie Cotter, University of Southern Queensland, Answer to question on notice, p. 4, received on 1 March 2016.

19 Professor Morris Altman, Dean and Head, Newcastle Business School, *Submission 12*, p. 4.

20 Professor Morris Altman, Dean and Head, Newcastle Business School, *Submission 12*, p. 4.

21 Co-operative Bulk Handling, *Submission 30*, p. 9.

Importantly, in agriculture or other industries with assets such as land, the active membership requirement promotes a community of interest, centring on an activity or type of business, typically within a region or locality, which is practised in similar form as between members. Dairy and irrigation farming are two simple and accurate examples of farming activity well-served by the co-operative model. A dairy farmer, for example must own land within a defined region and must carry on dairy farming at the location, in order to remain an active member. This reduces the risk associated with speculation, takeovers and asset-stripping and the emergence of oligopolies and monopolisation.<sup>22</sup>

### ***Committee view***

3.25 The committee notes the sector's potential contribution to the economy while still delivering for the community and continuing to provide its traditional sense of ownership for its membership. Nevertheless, the committee heard a consistent message from contributors that a cultural change is required in the financial trading and regulatory sectors in order to take full advantage of the co-operative model.

3.26 Globally the co-operative model is being utilised to tackle many of the issues facing the international community, from poverty to climate change. It is a model which is highly flexible and adaptable to local conditions and circumstances. The same is true in Australia. Sectors such as community health care or regional agriculture, where the mainstream market may not be able to service a community or provide the economy of scale required to compete nationally and internationally, are well suited to the model whereby community investment drives social enterprise to create sustainable business models.

3.27 The committee is also of the view that the sector should be included and supported to take full advantage of significant economic changes like the NDIS and the TPP. That said, the committee notes the aspirations of many co-operatives to develop and grow and this is always an admirable endeavour. However, the committee is cognisant that these developments offer an opportunity for communities to be at the centre of developments which affect them, which is the primary benefit of the co-operative model.

### **Recommendation 2**

**3.28 The committee recommends that co-operative and mutuals sector be better represented in government policy discussions, and is actively promoted as a possible option for service delivery particularly where community based initiatives are being considered.**

### **Recommendation 3**

**3.29 The committee recommends the Commonwealth Government work with states and territories to develop a program of supports to encourage the establishment of new co-operatives and mutual enterprises.**

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22 Kingfisher Law, *Submission 51*, p. 7.

## Recognition of mutuals

3.30 The recognition of mutuals is a different case than that for co-operatives. Whereas many co-operatives are smaller organisations that may require assistance from various levels of government in their establishment and governance; mutuals in Australia tend to be larger established enterprises that are looking for opportunities to expand and to ensure a level competitive playing field between themselves and traditional commercial companies.

3.31 A number of organisations made the point mutuals are ideally placed to complement government priorities as they both have interests and obligations beyond the economy. Australian Unity, a large mutual organisation urged the government to take advantage of what the sector has to offer both government and the broader community:

[M]y sense is that organisations such as ours can enter very useful dialogues with governments state and federal, because we have a more coincident set of interests...Our interests are aligned with communities, variously defined—communities of members. Often there is a coincidence of interests between government policy interests and the interests of our community. So I think there is an opportunity for natural alignment.<sup>23</sup>

3.32 Regis Mutual Management emphasised that the mutual model is well suited to address areas of potential market failure. They suggest that in those circumstances, when state assistance is requested or required, the mutual model should be promoted by government to facilitate communities working together to address those failings:

When markets fail, those affected often turn to State and Federal Governments for help. Governments can play an effective role in encouraging a sector or group of people to explore the mutual model as a means of overcoming a market failure. In other words, Governments can provide advice and support to affected groups so that they can help themselves...Government can assist by adopting policies that provide greater recognition and support to the roles of mutuals in society and the economy.<sup>24</sup>

## Defining the mutual corporate form

3.33 A central issue that was raised by a number of contributors was the lack of a legal definition of mutuals within the *Corporations Act 2001*. Australian Unity commented that :

...there is a barrier in terms of our corporate form not being sufficiently understood. I think that is one of the issues attaching to our original submission about a recognition in the federal Corporations Act in relation to this corporate form.<sup>25</sup>

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23 Mr Rohan Mead, Australian Unity, *Committee Hansard*, 30 October 2015, pp 6–7.

24 Regis Mutual Management, *Submission 33*, p. 2.

25 Mr Rohan Mead, Australian Unity, *Committee Hansard*, 30 October 2015, pp 6–7.



3.34 MAFIP Ltd. argued that the lack of a legal definition for a mutual has been a 'contributing factor to the low profile and their importance...'.<sup>26</sup>

3.35 Mutuals are regulated under the Corporations Act, however the mutual form is not defined in law. According to BCCM the mutual form requires better support in the Corporations Act to allow for more clarity for organisations operating under this legal model, including more clarity about the duties of directors.

3.36 Australian Unity placed the issue of defining mutuals within the Corporations Act at the top of their list of recommendations to develop the sector. According to their evidence the Corporations Act is currently tailored to govern for-profit companies where service is not a principal consideration:

The mutual form included in the Corporations Act seems to be almost there as an afterthought. The act is itself designed to govern companies limited by shares and organised for profit maximisation, rather than service maximisation. We argue that there is some inequity caused by this attempt to fit a square peg in a round hole, including the question of how to handle commercially valuable customer lists, which are different from shareholder lists as customers are often members.<sup>27</sup>

3.37 Bankmecu concurred with the call for recognition within the Corporations Act, suggesting that a definition is developed based on economic and governance tests. According to their submission this would bring a welcome coherency to the regulatory environment:

That the inquiry recommend that recognition of CMEs be given under the Corporations Act – defining mutuality with economic and governance tests. For example, not just regulatory guide (147) for transferring mutual financial institutions. This will give CMEs certainty and enable disparate state based regulations to be replaced with federal law.<sup>28</sup>

3.38 While accepting that the Corporations Act does not provide a legal definition for mutual enterprises, ASIC did explain that there is some guidance provided relating to de-mutualisation, and in that sense they have a fairly developed regulatory idea of what constitutes a mutual:

No; there is no legislative definition of mutuals, or a mutual. There is not one. For what are called 'transferring financial institutions'—so credit unions and societies that came from the state legislation or state supervision through to federal in the late nineties...there are enhanced disclosure provisions that relate to matters that might be called demutualisation; so just for those ones, not for mutuals generally. And we have given guidance around concepts of mutuality in relation to that part of the law, so we have a

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26 MAFIP Ltd., *Submission 46*, para 34.

27 Mr Rohan Mead, Australian Unity, *Committee Hansard*, 30 October 2015, p. 2.

28 Bankmecu, *Submission 18*, p. 2.

regulatory guide that sets out what we consider to be signs of being a mutual.<sup>29</sup>

3.39 To remove the current competitive barriers facing CMEs, Dr Gary Lewis, a co-operatives historian, recommended that specific federal legislation be developed for co-operatives, mutual and member-owned organizations (CMMOO) to take account of their 'democratic complexion':

I believe the formulation of simple, 'user friendly' federal legislation for CMMOO, perhaps as a section of the *Corporations Act* enshrining their democratic complexion, would be very helpful in removing barriers to innovation, growth and free competition for the sector in Australia.<sup>30</sup>

3.40 Australian Unity provided the committee with a proposed definition of mutuals that would 'help level the playing field when it comes to commercial governance':

Australian Unity believes "mutual" should be specifically defined in the Corporations Act as an entity:

- (a) being a body corporate where member liability is limited by the guarantee of its members (usually a nominal amount), rather than by share capital;
- (b) that operates an enterprise; and
- (c) in which membership (including any voting rights) is obtained as result of a person receiving a product or service or having another strong personal connection with the company such as an employment relationship, rather than by way of a formal application for membership (as distinct from think-tanks or charities) or an application for shares (as distinct from a body corporate limited by shares).<sup>31</sup>

### ***Mutuals - the role of directors***

3.41 In the event of the government amending the Corporations Act, many submitters recommended that the role of directors in mutual organisations be clarified. According to Australian Unity directors have very different obligations in a mutual structure and these need to be catered for in legislation:

[D]irectors of mutuals have different obligations to their constituents than those of shareholding companies. We argue that the service interests—providing the services and maximising those obligations for members—are an equally important consideration for directors of mutual organisations compared with economic interests for those who have ventured capital in

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29 Australian Securities and Investment Commission, *Committee Hansard*, 26 February 2016, pp 22–23.

30 Dr Gary Lewis, *Submission 36*, p. 3.

31 Australian Unity, *Submission 45*, p. 6.

shareholding forms. We have proposed a new definition of directors' duties to acknowledge this circumstance.<sup>32</sup>

3.42 Mr Matthew Koce, from hirmaa, shared the concerns of others in the sector that 'there needs to be recognition that the director's role is sometimes different in a mutual not-for-profit. That unique role needs to be recognised.'<sup>33</sup>

3.43 In addition to their proposed amendments to the Corporations Act to expressly define mutuals, Australian Unity provided the committee with proposed amendments to allow for all of a director's obligations in a mutual to be taken into account:

#### 12.3.01

This Part modifies the application of subsections 180(2)(a), 180(2)(d), 181(1)(a), 181(b), 184(1)(c), 184(1)(d), 187(a) and 187(b) of the Act in relation to the directors and officers of a company.

#### 12.3.02

A director or other officer of a corporation, in exercising their powers or discharging their duties, to act:

- (a) in good faith in the best interests of the corporation; and
- (b) for a proper purpose, should take into account the interests of members of the corporation as recipients of services provided by the company.<sup>34</sup>

3.44 While acknowledging that the role of directors in a mutual structure is broader in a mutual enterprise, ASIC considered that the current provisions in the Corporations Act would not necessarily exclude consideration of these broader duties when determining whether a director had acted in the best interest of the corporation:

[T]he directors' duties provisions in the Corporations Act are cast broadly. So directors need to act in good faith, in the best interests of the particular corporation, and it only obviously applies to cooperatives that are in corporate reform. So it is cast in a principled way, and it picks up a lot of the case law about the way judges have interpreted how directors need to act in particular circumstances. [A] judge in interpreting those provisions could look to: what is the purpose of this corporation? So if a corporation is in its constitution described as having particular goals, which may include cooperative or mutual goals, I think that would be a relevant consideration for a judge in applying that principle-based test...my observation would be that the way that the provisions are currently cast does have a degree of flexibility for judges in assessing whether or not someone is acting in the best interests of the corporation.<sup>35</sup>

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32 Mr Rohan Mead, Australian Unity, *Committee Hansard*, 30 October 2015, p. 2.

33 hirmaa, *Proof Committee Hansard*, 30 October 2016, p. 34.

34 Australian Unity, *Submission 45*, p. 10.

35 Australian Securities and Investment Commission, *Proof Committee Hansard*, 26 February 2016, p. 23.

3.45 Ms Ann Apps from Newcastle Law School accepted that the legislation does allow for a CME's co-operative principles to be considered in delivering a judgement, except in cases where there is a conflict between these principles and a director's financial obligations to the organisation:

The Act also provides that in interpreting any of its provisions, an interpretation which would promote the co-operative principles is preferred. However this does not address the problem that directors and managers face if required to defend a business decision which preferences social output (e.g. ethically sourced raw materials or better employment conditions for workers) at the expense of financial output.<sup>36</sup>

### *Committee view*

3.46 BCCM submitted a 'Mutuals Charter' which is a set of broad principles that, if followed by government, would provide a competitively neutral environment. The principles are:

- Co-operatives, mutuals and member owned businesses should be able to compete freely and on fair terms with all types of business
- Government should champion these business forms alongside other types of corporate ownership
- Government policy should recognise the value of these businesses and provide appropriate incentives for their creation and development
- Fiscal measures should promote co-operatives, mutuals and member owned businesses as much as share ownership of publically listed companies
- Legislation and regulation for these firms should match the best standards for any business
- It should be as cost effective and straight forward to set up and run a co-operative, mutual or member based businesses as any other type of business<sup>37</sup>

3.47 The committee concurs with the principles that support competitive neutrality. The committee heard repeatedly that the lack of a legal definition of mutuals was hampering its recognition and development. The mutual model is different but currently the Corporations Act, and its consequent regulatory framework does not take account of the features that differentiate the sector from other companies.

3.48 The committee is of the view that for the sector to be recognised and actively developed, it requires a concomitant regulatory structure. Being defined in law is a crucial step on the path to the sector being recognised more broadly.

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36 Ms Ann Apps, *Submission 28*, p. 5.

37 BCCM, *Submission 3*, p. 6.

## Recommendation 4

**3.49 The committee recommends that a mutual enterprise is explicitly defined in the Corporations Act 2001, and its associated regulations.**

3.50 A change to the Corporations Act's definition of duties for directors of mutuals would support a strengthening of governance in mutual organisations. By defining the corporate form, and by properly aligning directors' duties in that corporate form with the interests of members, outcomes for stakeholders would be improved.

## Recommendation 5

**3.51 The committee recommends that the role of directors in mutual enterprises be defined in the Corporations Regulations to align with the proposed definition of a mutual enterprise in the Corporations Act.**

## Establishing a co-operative

### *Cost and complexity of forming a co-operative*

3.52 The lack of recognition of CMEs as a viable model for people wanting to set up co-operatives has far-reaching implications for the sector. The committee received evidence that suggested this is an issue at local, state and federal administrative levels.

3.53 The number of members required to form a co-operative in Australia under the Co-operative National Law (CNL) is at least five at start-up. The basis of this requirement is not justified or explained in the bill's explanatory notes. A co-operative group (a co-operative of co-operatives) can be formed by two members, and the Registrar may give permission to enable a co-operative to start up with fewer than five members. The criteria for extending permission for fewer members is not published. Co-operatives can be formed under UK legislation with three members as a minimum.<sup>38</sup> A company can be formed with only one member. The section regulating membership is drafted in the NSW Act as follows:

(119)(3)The minimum number of members allowed is:

- (a) in the case of a co-operative group—2 co-operatives; or
- (b) in the case of any other co-operative:
  - (i) if a lesser number than 5 is approved by the Registrar—that number of active members; or
  - (ii) otherwise—5 active members.<sup>39</sup>

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38 In 1996 the Deregulation (Industrial and Provident Societies) Order 1996 SI 1996/1738 used the powers available to government under the Deregulation and Contracting Out Act 1994 to amend primary legislation by the use of regulations to reduce the minimum number of members needed to register a society from 7 to 3, the minimum number of members needed to register a society from 7 to 3. Co-operative News, *UK Co-op Law in 2010: A Summary*, available at: <http://www.thenews.coop/32865/news/banking-and-insurance/uk-co-op-law-2010-summary/>, (accessed 7 March 2016).

39 *Co-operatives (Adoption of National Law) Act 2012* (NSW), ss. 119(3).

3.54 The time required to register a co-operative was also raised by submitters. Prior to formation proposers must get approval for its rules/constitution by the Registrar. The Registrar may take up to 28 days to approve or reject or require amendment.<sup>40</sup> If the draft is rejected or amendment is required, then a further period of 28 days may be taken by the Registrar to approve. There are model rules provided under the legislation, however, guidance on matters such as the drafting of active member requirements is poor. The result is that it can take many months to gain approval or great cost to obtain professional legal advice to draft rules.

3.55 Evidence of the length of time it can take was provided by the Voluntary Parents Association who recounted their experience at the committee's hearing in Sydney, as well as in their submission:

Our co-operative took five months to register and cost over \$20,000 to establish, including \$17,000 of legal fees and several thousand dollars for various insurances. This is an enormous investment of time and money for a small not-for-profit.<sup>41</sup>

3.56 In their view the cost and regulatory burden is disproportionate for small non-profit and non-distributive co-operatives, and acts as a disincentive for people to establish co-operatives:

We understand and expect that Federal and State governments have a duty to protect consumers. However, we suggest a balance between protections and setting the bar so high that volunteers are discouraged from forming self-help organisations. From our perspective, half of the compliance work we did provided no meaningful protection to members. The problem is that government regulations are one size to fit all, from small worker co-operatives to large financial institutions, when the reality is that the needs and purposes of co-operatives within that spectrum vary widely.<sup>42</sup>

3.57 While there has been an improvement in the information and support available in those states that have adopted the Co-operatives National Law (CNL), there seems to be a persistent perception that there is lack of assistance in setting up a co-operative or seed funding a co-operative business available at a state or federal level.

3.58 The current advice on 'how to set up a small business' from governments at both a state and federal level only gives four types of business structure at most to choose from: sole trader, partnership, company and trust.

3.59 As mentioned above, there has been an improvement in information about co-operatives following the enactment of the CNL, but this is only available on the

40 NSW Fair Trading, *Registering a Co-operative*, available at: [http://www.fairtrading.nsw.gov.au/ftw/Cooperatives\\_and\\_associations/Registering\\_a\\_cooperative.page](http://www.fairtrading.nsw.gov.au/ftw/Cooperatives_and_associations/Registering_a_cooperative.page) (accessed 7 March).

41 Voluntary Parents Association, *Submission 37*, p. 7; *Committee Hansard*, 29 October 2015, pp 1–2.

42 Voluntary Parents Association, *Submission 37*, p. 7.

co-operative section of the government's website, not in the small business section. The system therefore assumes some form of pre-existing knowledge when someone wants to set up a co-operative, or that a co-operative may be the most appropriate option for their enterprise.

3.60 BCCM provided an example whereby government firstly does not consider co-operatives in the development of policy, and then government officials do not have knowledge of whether co-operatives are eligible for the subsequent program:

It seems to pop up in lots of different places[...]we received an inquiry about a current tax exemption program that was being offered to R&D organisations. This was to encourage the flourishing of entrepreneurship and start-ups. [T]his group had been turned down for the program for the exemption based on the fact that they were not a corporate entity that was recognised within the program. When we tested it, we went through three layers of people—officers of the department—and were rejected. When we finally pushed it—eventually we received a ruling that, in fact, cooperatives were eligible. So this really is endemic throughout the system...<sup>43</sup>

3.61 However, as discussed above and in Chapter 2, the committee found that those states and territories which have adopted the CNL have significantly improved the information available on establishing co-operatives. The Australian Tax Office also provided the committee with information showing the relatively straightforward steps someone would have to take to apply for an ABN as a co-operative.<sup>44</sup>

### ***Improving education, knowledge and expertise***

3.62 Other submitters contend that a lack of education about CMEs in tertiary institutions, compounds the problem for co-operatives in getting appropriate advice since there is a lack of professional business advisors with requisite knowledge of the business models. The Co-operative Bookshop also raised the lack of understanding in the professions generally tasked with advising organisations on aspects of governance:

Co-operatives and mutual enterprises (CMEs) are poorly understood due to the paucity of education provision; leading to under-recognition of the business model by key professions including accounting and legal practitioners.<sup>45</sup>

3.63 Ernst and Young (EY) were of a similar view that the lack of expertise in the relevant professions as well as government agencies was hindering the development of the sector:

The CME sector does not have access to the same level of government and professional support for the model because of lack of specialised expertise. There is therefore a need to develop this expertise across relevant

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43 Ms Melina Morrison, Business Council of Co-operatives and Mutuals, *Committee Hansard*, 30 October 2015, p. 22.

44 Australian Tax Office, answer to question on notice, received 8 March 2016.

45 The Co-operative Bookshop, *Submission 38*, Attachment 1, p. 1.

government agencies and professional advisors in order to facilitate the establishment and growth of CMEs.<sup>46</sup>

3.64 While agreeing there is a serious deficiency in the expertise available to CMEs, Professor Greg Patmore did suggest that renewed focus as a result of the UN International Year of Co-operatives has made a difference in bringing forth improvements in the training of those professionals tasked with advising the sector:

The co-operative sector is largely ignored in both secondary and tertiary education which limits knowledge about the co-operative business model. In the wake of the Cooperative, mutual and member-owned firms UN International Year of Co-operatives there has been some interest in including cooperatives in the tertiary curriculum of business students.<sup>47</sup>

3.65 The sector itself is attempting to address the lack of understanding and expertise across the professions by establishing links with the tertiary education sector to ensure that more is being done to improve the understanding and awareness of the cooperative model. The Co-op Bookshop highlighted the progress being made so far, with a number of universities introducing and developing courses for law, accountancy and other relevant students on the model:

A number of Universities have embarked on development and actual introduction of courses including, Newcastle University, University of Western Australia, Charles Sturt University and Sydney University. While these steps are positive, more needs to be done to ensure an understanding of the CME model by legal practitioners, accountants, and other service providers. Inclusion of the CME business model in business-related courses at all levels of education would significantly assist in raising awareness of the sector in the Australian economy.<sup>48</sup>

3.66 The Mercury Centre said that they were often approached by prospective cooperatives who say they are often counselled not to go down the cooperative path by accountants and lawyers who do not have the requisite knowledge of the model to properly advise them:

The Mercury Centre is responding to regular requests flowing from workshops that the ability and expertise to set up Cooperatives is not available. Consequently communities are regularly dissuaded from the cooperative path by accountants and lawyers who do not have the knowledge to set up cooperatives and recommend alternatives such as shelf Pty Ltd or Incorporated Associations.<sup>49</sup>

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46 Ernst and Young, *Submission 44*, p. 2.

47 Professor Greg Patmore, *Submission 4*, p. 17.

48 The Co-operative Bookshop, *Submission 38*, p. 10.

49 Mercury Centre, *Submission 43*, p. 7.



3.67 This view was backed up by the Cohousing Cooperative who claimed that they have 'ongoing difficulty working with both these professions [accountancy and lawyers], as there is a lack of knowledge of co-operatives as a legal structure.'<sup>50</sup>

3.68 Furthermore, the Centre argued that this lack of expertise among the professions of law and accountancy added to both the burden of governing a co-operative, and to the cost:

It is a commonly held view that establishing and maintaining a Cooperative is a more expensive and onerous task than the compliance for a Propriety Limited (Pty Ltd) or Incorporated Association. This position is exacerbated by the lack of inclusion and professional training at tertiary level in Law and Accountancy.<sup>51</sup>

3.69 Kingfisher Law were also of the view that the current provision in tertiary courses and professional development for those who are expected to provide advice and expertise to the sector is limiting its progress and hindering the concomitant benefits to the broader economy:

Australian entrepreneurs and managers, financial advisers, regulators, lawyers, accountants and elected representatives need increased access to better, more accurate information on, and expertise for, co-operatives and mutuals. Without this, Australia risks foregoing optimal development, which would otherwise be achievable.<sup>52</sup>

3.70 In contrast, a response to a question on notice from the committee, the Head of Education at Chartered Accountants Australia New Zealand said that in his experience the exact opposite was the case:

I have spent most my career working for, or being a director of co-operatives or mutuals (CAANZ is one). I can say that my general background in accounting made it quite easy to take on those duties and I had no difficulties in acting as a director and coping with the particular structure of a co-operative. I think that would be true of accounting professionals generally. The co-operative structure is not difficult to understand and the conduct of the business of at least most co-operatives is not very different from those of other businesses... I have seen no evidence of an issue with advisors with the requisite knowledge, indeed my experience is the reverse and that the market responds to needs for advice very efficiently.<sup>53</sup>

3.71 According to the BCCM, the ramifications of this lack of expertise do not just impact the establishment or development of a CME, they can also result in regulations or tax law being misapplied, and have serious consequences for the CME:

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50 Cohousing Cooperative, *Submission 7*, p. 2

51 Mercury Centre, *Submission 43*, p. 5.

52 Kingfisher Law, *Submission 51*, p. 3

53 Chartered Accountants Australia and New Zealand, answer to question on notice, received 11 March 2015.

Co-operative and mutual business forms are not well understood by policy makers, lawyers and accountants or other business advisors. As a result, business advice for those wishing to set up a co-operative or mutual is inconsistent and ad-hoc at state level, and too often, the different business purpose that mutuals have is ignored, leading to inappropriate regulation and treatment from authorities.<sup>54</sup>

### ***Committee view***

3.72 The introduction of the Co-operatives National Law in most states and territories has resulted in improvements to the advice, guidance and information available to those wanting to set up and govern co-operatives. The committee welcomes these improvements and with the rollout of the CNL, or equivalent legislation across the whole country, expects similar improvements in all jurisdictions.

3.73 The committee notes the role of regulatory bodies in ensuring that co-operatives are not being ill-advised is central to the role of government at all levels. The evidence received by the committee about co-operatives incurring additional costs because of inappropriate advice is something those responsible for registering and regulating co-operatives should be aware of, and seek to mitigate where possible.

### **Recommendation 6**

**3.74 The committee recommends the Commonwealth Government work with states and territories to ensure the continual improvement to advice, guidance and information provided at all stages in the establishment, governance and regulation of co-operatives.**

3.75 The committee is particularly interested in strengthening the educational curriculum to underpin the development of the sector. Without access to expertise to guide co-operatives through establishment, governance, regulation and compliance, the potential of the sector is always going to be limited.

3.76 The committee is cognisant of the advances in this field, with several universities offering units within their law and accountancy courses. Recent examples, such as the commitment in the Agriculture White Paper to offer training courses on 'cooperatives and other business structures to help farmers to better engage through the supply chain and attract investment', are proof that government can have a role in developing the sector at this level.

3.77 Nevertheless, there is still significant capacity in the secondary and tertiary education field to increase awareness of the CME model. Moreover, there is also capacity for increased professional recognition in courses from relevant professional bodies such as accountancy bodies, the Institute of Company Directors to teach students about diverse business ownership models.

3.78 While the committee understands that it is not the government's role to set curriculum in tertiary institutions, or private industries bodies, it urges the government to facilitate in whatever way it can to improve the situation. The committee would

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54 Business Council of Co-operatives and Mutuals, *Submission 3*, p. 19.

also encourage greater liaison between the CME sector and the tertiary institutions and peak bodies to promote the value of improving recognition of the sector within tertiary institutions.

### **Recommendation 7**

**3.79 The committee recommends that the Commonwealth Government work with all relevant stakeholders to undertake a program of education and training to inform all stakeholders about the role of co-operatives and mutuals.**

### **Recommendation 8**

**3.80 The committee recommends that the Commonwealth Government examine ways in which it can improve the recognition and understanding of the co-operative and mutual sector in the national secondary school curriculum, and that tertiary institutions consider the inclusion of co-operatives and mutuals in accounting, business, commerce, economics and law degrees.**

### **Recommendation 9**

**3.81 The committee recommends that professional accreditation bodies, such as the Law Society and Institute of Chartered Accountants, require a demonstrated knowledge of the co-operative and mutual structure before they will licence its members to practice accounting or law.**

### **Issues affecting Indigenous co-operatives**

3.82 The committee received evidence from Indigenous co-operatives which share similar concerns to other CMEs, but which also have specific issues relating to Indigenous organisations' eligibility to access government funding as a co-operative.

3.83 Academic research submitted to the inquiry on the experience of Indigenous communities in establishing co-operatives, shows a lack of recognition of the contribution of co-operatives in Indigenous communities, and that many of them did not receive any support while setting up the enterprise.<sup>55</sup>

3.84 The committee heard evidence citing Tranby College in Sydney as an example of a long running co-operative that had received excellent results for its members and broader community since its establishment in the late 1950s:

Tranby Aboriginal College in Sydney, the training and educational arm of Cooperative for Aborigines Ltd, which has been operating successfully since 1958, is an excellent model demonstrating what can be achieved with a diverse group of students from all around Australia, including remote regions, studying in a supportive and cooperative environment while emphasizing indigenous ownership and control.<sup>56</sup>

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55 Associate Professor Branka Krivokapic-Skoko, Charles Sturt University, *Submission 13*, p. 2.

56 Dr Gary Lewis, *Submission 36*, p. 3.

3.85 Evidence suggests the co-operative model is ideal in delivering services in remote areas, such as Indigenous communities, where issues can be complex and service provision through the private sector is often not suitable or available:

Awareness of multi-stakeholder CME structures may open up opportunities for developing effective governance structures for managing complex problems including those experienced by organisations delivering public services and those operating in Indigenous communities.

The owner member characteristic especially when a multi-stakeholder structure is utilised may be particularly effective governance model when addressing complex problems and where CMEs facilitate community empowerment. There may be opportunities to use multi-stakeholder structures in Indigenous communities or as the basis for collective impact initiatives which seek to harness diverse resources to achieve a common goal.<sup>57</sup>

3.86 Despite their apparent suitability to deliver services through community ownership in communities, the committee heard that many co-operatives are being pressured to convert to corporations in order to access government funding. Councillor Kanak gave evidence to the committee in Melbourne and explained his statement in his submission that:

A current barrier to innovation, growth, and free competition in the Aboriginal Torres Strait Islander Community is the funnelling of Aboriginal Torres Strait Communities away from co-operative models towards Aboriginal corporations, albeit in an atmosphere of purported freedom of choice.<sup>58</sup>

3.87 Mr Wy Kanak from Tranby College informed the committee that, under the Indigenous Advancement Strategy, Commonwealth Government grant funding above \$500 000 was only available to Indigenous organisations incorporated under the *Corporations (Aboriginal and Torres Strait Islander) Act 2006*.<sup>59</sup> According to Mr Kanak this is causing deep distress in co-operatives such as Tranby College and may cause them to 'abandon their cooperative structure and reincorporate under the Aboriginal Councils Act'.<sup>60</sup>

3.88 A similar issue was raised in the inquiry that wasn't specific to Indigenous organisations. The Master Butchers Co-operative Ltd informed the committee that the Next Generation Manufacturing Investment Programme stipulates that eligible applicants must be 'an entity incorporated under the Corporations Act 2001'.<sup>61</sup>

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57 Ernst and Young, *Submission 44*, p. 3.

58 Councillor Kanak, *Committee Hansard*, 29 October 2016, p. 64.

59 Australian Government, *Indigenous Advancement Strategy Guidelines, Part 2.8.2*, July 2014, p. 8.

60 Mr Wy Kanak, *Committee Hansard*, 29 October 2015, p. 64.

61 Master Butchers Co-operative Ltd, *Submission 60*, pp 1–2.

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***Committee view***

3.89 The committee was concerned to hear that funding streams to previously successful Indigenous co-operatives were placed in jeopardy by the obligation for grant recipients above a certain level to be corporations. Not only does this restriction cause angst in the organisations and communities they support, it also sends the wrong signal to the co-operative sector more generally. Amending the Indigenous Advancement Strategy to allow co-operatives registered under the CNL would alleviate funding concerns, and demonstrate recognition of the value the sector brings to Indigenous communities.

3.90 The application of these restrictions across government grants and funding mechanisms further concerns the committee. This is a tangible example of co-operatives being disadvantaged against other types of business structures and the committee is keen to understand why these restrictive practices are in place. While the committee understands that governments must ensure appropriate risk management strategies are in place when expending public funds, there appears to the committee to be no compelling reason why co-operative and mutual enterprises present any more risk than incorporated organisations. In the absence of any justification the committee is of the view the restrictions should be removed.

**Recommendation 10**

3.91 **The committee recommends that the Commonwealth Government amend the Indigenous Advancement Strategy to allow registered co-operatives the same access to allow levels of grant funding as other entities.**

**Recommendation 11**

3.92 **The committee recommends that the Commonwealth Government review, and where necessary amend the eligibility criteria for grants and funds across all government grants and program guidelines to ensure that co-operatives and mutual enterprises are not excluded on the basis of their business structure.**



## Chapter 4

### Regulation and access to capital

4.1 This final chapter discusses the regulation of the sector, and whether it provides competitive neutrality, and issues raised by the sector around access to capital.

#### Regulation

4.2 The Australian Uniform Co-operative Laws Agreement (AUCLA) committed jurisdictions to uniformity of regulation. While most states and territories have adopted the legislation, or committed to introducing consistent legislation, full uniformity has not yet come to fruition.

4.3 The sector is governed by a plethora of regulations and bodies, depending on what type of co-operative or mutual it is. Dual regulation and registration across federal and state jurisdictions also remains in some cases. Ernst and Young described the current regulatory environment:

Cooperative organisations have been registered and regulated by State and Territory governments, with the exception of financial cooperatives. Credit unions, mutual building societies and friendly societies are not covered by the Cooperatives National Law [CNL]. These organisations are Authorised Deposit-taking Institutions and are federally regulated as Australian banks. [Co-operative and Mutual Enterprises] CMEs which are non-distributing including those that are Public Benefit Institutions (PBIs) are regulated by the Australian Charities and Not-for-Profit Commission (ACNC).<sup>1</sup>

4.4 Many submitters expressed concern that the current regulatory burden was not flexible enough to cater for all sizes and types of CME. While one of the goals of the CNL is to reduce reporting requirements for small cooperatives<sup>2</sup>, this is apparently not being felt by organisations at that level. The Voluntary Parents Association suggested that the regulatory environment is over-burdensome for small co-operatives, and should be flexible enough to allow all sizes of CMEs to operate:

To be clear, we do not challenge the need for an authority like the ACNC, or the objectives of NSW Fair Trading, but we do ask that there be some recognition that small not-for-profit self-help groups do not have the resources to fulfil obligations that seem small to others, and that some leeway be granted or streamlining created. It is surely not impossible for standard information on co-operatives, such as names, registration details,

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1 Ernst and Young, *Submission 44*, pp 21–22.

2 These are defined as cooperatives which do not raise funds through the public issue of securities and meet several criteria on size of entities, assets, and number of employees. (EY, *Submission 44*, p. 22.

ABN's, to be shared and allowed to populate the forms that each government department requires.<sup>3</sup>

### **Dual registration**

4.5 Ms Robyn Donnelly expressed concern about the lack of consistency across different jurisdictions, which resulted in duplicity across many regulatory requirements. According to Ms Donnelly, this is not only an issue in the application of the CNL, but also in the policies in relation to registration across state lines and interstate fundraising:

There is no uniform administrative policy across those jurisdictions that have commenced the law. There has been no progress in removing dual regulatory requirements for cooperatives that are imposed as a result of the operation of the Corporations Act on interstate transactions by cooperatives. Those are in the areas of issuing securities across state and territory borders and also the requirement for registration under part 5B.2 of the Corporations Act.<sup>4</sup>

4.6 ASIC confirmed that if a registrable Australian body wishes to carry on business in one or more states or territories other than its home jurisdiction, it must be registered under Part 5B.2 of the Corporations Act. An association which is registered under a state law not recognised in other states will generally be a registrable Australian body. A foreign company wishing to carry on business in Australia must be registered under Part 5B.2 of the Corporations Act.<sup>5</sup>

4.7 Many co-operatives are registered under both state laws, and under Part 5B.2 of the Corporations Act which prohibits the carrying on of business by a state registered body (a co-operative) outside its state of origin unless it registers under Part 5B.2. The Business Council of Co-operatives and Mutuals (BCCM) propose that co-operatives should be exempt from this dual-regulatory requirement.<sup>6</sup>

4.8 The Australian Securities and Investments Commission (ASIC) further explained that dual registration may be a requirement of both the *Corporations Act 2001* and the CNL. While there are aspects of the Corporations Act that exclude participating co-operatives under the CNL, the decision not to exclude them from registration requirements under both Acts seems to be a deliberate policy decision:

Under section 12(1) of the Appendix to the Co-operatives (Adoption of National Law) Act 2012, a co-operative and a participating co-operative are each declared to be an excluded matter for the purposes of section 5F of the Corporations Act 2001 (Cth) in relation to the whole of the Corporations legislation. However section 12(2), subsection 12(2)(1)(c) does not exclude the application of the Corporations legislations to co-operatives or participating co-operatives to the extent that the provisions relate to the

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3 Voluntary Parents Association, *Submission 37*, pp 6–7.

4 Ms Robyn Donnelly, *Committee Hansard*, 29 October 2015, p. 7.

5 ASIC, Answer to question on notice, received 10 March 2016.

6 Business Council of Co-operatives and Mutuals, *Submission 3, Attachment 2*, p. 24.



registration of a co-operative as a company under Chapter 5B of the Corporations Act. In other words it appears there was a deliberate policy decision made to apply both regimes.<sup>7</sup>

### ***Dual fundraising regulation***

4.9 Under s708 (20) and s66A of the Corporations Act, a security – share or debt security – issued by a co-operative is an exempt security if it is offered or issued within its state of origin. As an exempt security, these offers are not subject to the disclosure requirements. However they are subject to the disclosure requirements of the state legislation (CNL or Co-operatives Acts). The disclosure requirements for debt securities issued by a co-operative match the disclosure requirements for similar securities under the Corporations Act.

4.10 However, if a co-operative offers any security to persons in another state or territory, then it must comply with the disclosure requirements under the Corporations Act. This will require the lodgement of a disclosure document or an application for exemption from ASIC. This exposes a co-operative to double lodgement fees and potentially double preparation costs. BCCM outlined the lack of a coherent system between jurisdictions, as well as between regulatory bodies:

There are instances of dual and inappropriate regulatory compliance obligations for co-operatives. As a result of the division of regulatory authority for corporations and financial markets, co-operatives that wish to issue shares or other securities where a potential subscriber resides in another state or territory must comply with disclosure requirements under both state co-operatives legislation and disclosure regulations developed for investor-owned companies under the Corporations Act.<sup>8</sup>

4.11 Ms Robyn Donnelly discussed the potential risk of dual regulation in terms of the disclosure requirements for co-operative shares:

The CNL provides for disclosure in respect of the issue of shares in a co-operative based on the nature of these securities. The disclosure requirements for shares in a company are different and are not appropriate for the issue of shares in a cooperative. However, a co-operative wishing to issue shares as part of a membership offer across a state border is subject to the disclosure requirements for the issue of shares by a company under the Corporations Act.

The disclosure requirements for company shares are both unsuitable for cooperative shares and constitute dual and potentially costly regulation.<sup>9</sup>

4.12 While ordinarily a non-distributive co-operative is not required to lodge a disclosure statement, the Registrar does have discretion to require one be prepared. There appears to be no policy or guidance about whether such a document will be required, and as such, proposed co-operators do not know whether to prepare for this

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7 ASIC, Answer to question on notice, received 10 March 2016, pp 2–3.

8 Business Council of Co-operatives and Mutuals, *Submission 3*, p. 22.

9 Ms Robyn Donnelly, *Committee Hansard*, 29 October 2015, p.7.

as they may be required to prepare such a document at a later date. This adds to the time it takes to form a co-operative and the cost.

4.13 The Voluntary Parents Association were concerned that the disclosure requirements were out of sync with the overall registration process, and were too onerous for small co-operatives more generally:

For us in forming the co-operative we felt it was strange that we had to write a disclosure statement that identified who the directors were before we had an election for the board and to declare who the General Manager was before we had raised funds to look for someone to fill the position.

We ask that regulatory bodies scale the level of regulation to the size of the co-operative. Whilst there would be argument that this would increase the cost for the regulator, what we are doing currently is to pass on that cost to the co-operative, which is not in an easy situation to cover such costs.<sup>10</sup>

4.14 ASIC responded to a number of questions on notice generally about the regulatory burden on co-operatives. With regard to the claims of duplication around the disclosure requirements for interstate offerings of securities under Chapter 6D of the Corporations Act, ASIC stated that if the shares being offered were member shares, and were not to raise capital, then they wouldn't be subject to these requirements:

If the shares being offered are to members, and it is not an issue to raise capital, to raise money, then chapter 6D would not apply. Chapter 6D of the Corporations Act applies when someone is issuing shares to receive money in as capital formation, whether it is shares, other securities, debt instruments or otherwise.<sup>11</sup>

### ***Committee view***

4.15 There is duplication in both registration and disclosure regulation across state and regulatory lines. The regulatory framework that governs fundraising, disclosure, registration and compliance for CMEs can be burdensome, particularly for small and medium sized CMEs. These CMEs operate very differently from companies and the committee is keen to ensure that they are appropriately regulated relative to their size and operation.

4.16 The committee also heard calls for the burden of regulatory policy proposals on co-operatives and mutuals to be specifically considered. While this is a complex area, the committee is supportive of calls by the sector to be treated in the same way as other types of business.

### **Recommendation 12**

**4.17 The committee recommends that the co-operative and mutual sector be considered when the government is preparing a Regulatory Impact Statement that accompanies new regulatory policies.**

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10 Voluntary Parents Association, *Submission 37*, p. 9.

11 ASIC, *Proof Committee Hansard*, 26 February 2016, p. 23.

## Recommendation 13

**4.18 The committee recommends that the Commonwealth Government liaise with its state and territory counterparts to ensure that the regulatory burden for small and medium sized co-operative and mutual enterprise aligns with the needs of these organisations and ensures they are not disadvantaged relative to companies of a similar size.**

4.19 With respect to the issue of disclosure of interstate offerings of securities, the committee is of the view that if an organisation is behaving ostensibly in the same way as a company then they should be similarly regulated.

4.20 On the issue of dual registration of CMEs who are operating interstate and as such are required to register under both the CNL and the Corporations Act, this appears to be a deliberate decision taken and agreed by all the states and territories that have so far enacted the legislation. While all aspects of the Act should be reviewed periodically to ensure they are achieving their respective outcomes, the committee is of the view that it is appropriate to wait until all jurisdictions have legislation in place before this review takes place.

## Accessing capital

### *Accounting standards - measuring the true value of a co-operative*

4.21 The committee heard that one of the barriers for a co-operative or a mutual to access capital is how their balance sheets are represented. A member of a co-operative has voluntarily contributed their shares in the enterprise, and is entitled to a full refund of their contribution should they leave. Current accounting standards therefore treat their shares on the balance sheet as a liability rather than equity. BCCM highlighted the unintended consequences of this accounting treatment:

Australian Accounting Standards have incorporated International Financial Reporting Standards developed to provide consistent information for investor-owned firms. These financial reporting standards were applied in 2005 to all reporting entities regardless of whether they are investor-owned or member-owned. The result of the application of these standards to CMEs was dramatic. The different nature of a share in a co-operative or a mutual meant that it was classed as a liability whereas in a company it was classed as equity. Virtually overnight, many CMEs with a share capital were rendered undercapitalised.

4.22 Furthermore, BCCM suggested the financial standards and practice are not adequate to measure the true economic benefit to the economy, with the community impact of the work of co-operatives being ignored, and not adequately measured by current accounting methods:

International developments for Integrated Reporting to include greater emphasis on intangible assets of an enterprise such as human, social and natural capital dictates the need to focus on broader value measurements. Standard financial and accounting metrics are inadequate to capture their full value. Research by Ernst & Young in 2014 shows that for every \$1

spent in a co-operative enterprise 76% of value was added to its community.<sup>12</sup>

4.23 This is a view shared by Ms Ann Apps, a law academic from Newcastle Law School, who says the problem is compounded by the Co-operatives National Law itself because does not present the true value of CMEs because the accountancy treatment they receive is based on the reporting requirements of the Corporations Act which are not appropriate for the co-operative model:

The CNL adopts financial auditing and reporting requirements that are largely based on the reporting requirements found in the Corporations Act.<sup>15</sup> It has been acknowledged that ‘fair value’ accounting fails to provide an accurate or holistic representation of how organisational value is created over time...The inability of financial metrics to capture the social value of CMEs and the operation of Financial Reporting Standards results in inadequate recognition of the value and importance of the CME sector.<sup>13</sup>

4.24 In response to questions on notice about whether there is any way that accounting standards could be amended to avoid co-operatives recording their shares as liabilities, Chartered Accountants Australia and New Zealand informed the committee that possible solutions to the problem were being mooted by the International Accounting Standards Board (IASB):

The International Accounting Standards Board (IASB) is currently undertaking a project on *Financial instruments with the characteristics of equity*. The final outcomes of this project may include possible solutions to bring co-operative shares within the definition of capital under AASB 132.

The IASB’s current investigations include potential improvements to (1) the classification of liabilities and equity in IAS 32 *Financial Instruments: Presentation*, including investigating potential amendments to the definitions of liabilities and equities in the *Conceptual Framework*; and to (2) the presentation and disclosure requirements for financial instruments with characteristics of equity, irrespective of whether they are classified as liabilities or equity.<sup>14</sup>

### ***Committee view***

4.25 The ability for a co-operative to compete on an equitable basis with other business structures, and meet its established objectives, is contingent on the appropriate application of financial instruments such as Accounting Standard IAS 32. The committee therefore welcomes the developments at the IASB which may provide solutions to the consequences of the application of current accounting standards.

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12 BCCM, *Submission 3*, p. 15.

13 Ms Ann Apps, *Submission 28*, p. 6.

14 Chartered Accountants Australia and New Zealand, answer to question on notice, received on 9 March 2016.

## Recommendation 14

4.26 **The committee recommends that the Commonwealth Government closely monitor the progress of the International Accounting Standards Board in developing solutions to bring co-operative shares under the definition of capital under AASB 132, and, where possible, facilitate equivalent amendments as expeditiously as possible.**

### *Access to capital*

4.27 Access to capital was cited as a significant problem for CMEs. The issue is that all mutuals are established for a purpose and are owned by their members, and no one can take away their share of the assets unless the entity is demutualised. Mutuals therefore have no shares they can sell or trade and have no access to the equity markets.<sup>15</sup>

4.28 Organisations from the agricultural sector argued that their sector in particular has problems investing in essential infrastructure:

A major issue that Norco faces is the availability of capital for infrastructure projects. Other than traditional bank debt, there is little opportunity to seek large amounts of capital to upgrade infrastructure from our members given the economic conditions they face as primary producers. Even though Norco can shield our members from the supply and demand issues they would face if trying to market their produce individually, there is still very little margin left due to ever-increasing production costs and so any compulsory contribution schemes approved under the Co-operative National Law are for modest amounts at the most.<sup>16</sup>

4.29 Professor Cotter from Southern Queensland University informed the committee of research currently being undertaken to examine how agribusiness co-operatives can access further amounts of capital:

To address the issue of access to capital for expansion of the sector, we have commenced research into capital raising for agribusiness including available and emerging co-investment models, including investors are looking for and governance considerations. There is a lack of knowledge amongst agribusiness enterprises about access to equity capital. Further, lack of sufficient scale and compelling business cases limits the number of investable farming and agribusiness enterprises. Investors include managed funds, private equity, high net worth individuals and family offices.<sup>17</sup>

4.30 Ms Ann Apps proposed the legal recognition of an alternative, or 'hybrid' CME that could have greater access to capital. According to Ms Apps, a 'pure' co-operative that allocates control rights to active members under the principle of one

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15 Employee Ownership Australia Ltd, *Submission 23, Attachment 1*, The Ownership Commission 2012, p. 78.

16 Norco, *Submission 9*, p. 2.

17 Professor Julie Cotter, *University of Southern Queensland*, answer to question on notice, received 1 March 2016.

member, one vote, was sacrificing the ability to access external capital for democracy.<sup>18</sup>

4.31 Ms Apps suggested that this model could be supported by changes throughout the regulatory framework to enable the diversity of business models beyond the traditional definitions that exist in state and federal legislation:

There is a general lack of understanding of the key legal features of the co-operative model and the importance of protecting the legal distinction between the co-operative and the company models. However there is a case for diversity of business models including the separate legal recognition of a 'hybrid' co-operative company under the *Corporations Act 2001* (Cth).<sup>19</sup>

4.32 The Australasian Mutuals Institute submitted that the implementation of more stringent regulation following the Global Financial Crisis (GFC) has benefited larger banks, but inhibited access to capital for smaller banks and customer owned banks:

In summary there has been a continual flow of outcomes post the GFC that has advantaged the major banks and disadvantaged regional banks and customer owned banking institutions competitive position in the market thereby reducing important choice for the Australian consumer. This has been further exacerbated for the customer owned banking institutions by the prudential regulator's approach to Basel III implementation which has served to severely limit their access to capital instruments that align to mutuality.<sup>20</sup>

4.33 Ernst and Young provided the committee with specific suggestions for ways in which CME's could improve their access to capital, primarily within the sector itself:

- There needs to be greater awareness of the alternative methods for CMEs to access capital amongst CMEs themselves, financial institutions and rating agencies.
- Templates need to be developed based on the Cooperative National Law and successful capital raising mechanisms to reduce the costs of capital raising and speed-up the process.
- Mature CMEs have the potential to explore opportunities for research and development and the investment in other CMEs.
- Establish a Cooperative and Mutual Development Investment Fund controlled by CMEs may increase the access to capital for new and growing CMEs.<sup>21</sup>

4.34 Submitters cited other jurisdictions like the UK, Canada and the Netherlands as having recognised the value for the economy of diverse corporate structures. The

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18 Ms Ann Apps, Newcastle Law School, *Submission 28*, p. 4.

19 Ms Ann Apps, Newcastle Law School, *Submission 28*, p. 4.

20 Australasian Mutuals Institute, *Submission 20*, p. 5.

21 Ernst and Young, *Submission 44*, p. 3.

Mutuals Deferred Shares Act in the UK was highlighted as a possible model to allow investment for growth by mutual organisations. Australian Unity recommended that Australian law and regulation be amended to allow similar opportunities:

In jurisdictions such as these, corporate regulation exists which defines and permits (and importantly, does not preclude) the issue of financial securities by mutuals, for example by the Mutuals Deferred Shares Act in the UK.

Australian Unity submits that Australian law and regulation be amended to enable the issue of such securities by mutual organisations. Consideration should also be given to the opportunity to permit franking for the returns on such instruments in the Australian context. This would allow tax-paying mutuals to utilise currently unusable franking credits and would also remove yet another competitive disadvantage for these types of mutual companies versus typical shareholding companies.<sup>22</sup>

4.35 The National Health Co-operative also cited the UK's legislative changes as a model that Australia could look at further:

There is a precedent in the United Kingdom which you may be aware of. They passed a new act of parliament—about a year ago, I understand—that enables cooperatives to issue capital-raising rounds. It is treated in much the same way as any other capital-raising round would be treated. The dividend paid to those investors is considered equivalent to interest paid on a loan—it does not change the risk profile, if it is managed appropriately. It is something that this government could look at.<sup>23</sup>

4.36 Australian Unity further submitted examples of novel capital instruments in the Australian context, and argued that these are examples of mutuals raising long term capital with a fixed return, and all that has been missing in Australia is 'a clearly legislated invitation to mutuals to follow that path':

Currently in Australia, APRA regulations (APS 111) envisage the conversion of Additional Tier 1 (AT1) and Tier 2 (T2) debt capital instruments held by Authorised Deposit-Taking Institutions (ADIs) into Mutual Equity Interests (MEIs) upon a loss absorption or non-viability event. The MEIs are not envisaged to be shares under the Corporations Act, although that has not yet been tested in court, and they would be able to be redeemed on a winding up but at no more than the face value of the original instrument. While this kind of capital cannot be deliberately created—it only arises on a negative trigger event—it is a contemporary Australian example of a regulator considering a new capital instrument that did not previously exist for mutual organisations.<sup>24</sup>

4.37 In response to specific questions on notice about the status of Mutual Equity Interests (MEIs) under the Corporations Act, ASIC responded:

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22 Australian Unity, *Submission 45*, p. 12.

23 National Health Co-operative, *Committee Hansard*, 26 February 2016, p. 4.

24 Australian Unity, *Submission 45*, p. 12.

Mutual ADI's do not issue MEIs directly as a form of capital, but may end up with MEIs in their capital structure if they are required to convert their hybrid instruments. MEIs may result from a hybrid regulatory capital instrument issued by a mutual ADI that is required to convert – with MEIs issued on conversion rather than ordinary shares.

The aim of MEIs is to provide the Mutual ADIs with access to convertible regulatory capital in the same way that other ADI's have used convertible hybrids. MEIs were contemplated by APRA in Attachment K to Prudential Standard APS 111. It is anticipated the specific terms of the particular MEIs are to be included in the constitution of the mutual proposing to issue them.

It is not possible to answer specifically how MEIs would be treated under the Corporations Act as no instruments that have the possibility of converting to MEIs have been issued to date. Like hybrids there are no standard terms for the instruments that may give rise to MEIs or for the MEIs themselves. The determination will depend on the specific structure and form of the instrument (pre conversion) and the form of the MEI post conversion.

If the pre-conversion instrument and/or the MEIs into which they may convert are considered preference shares, then member approval requirements of Part 2H.1 of the Corps Act would apply. If both the pre-conversion instrument and subsequent MEI are legal form debt – then the instrument may not require member approval. Given that mutuals are likely to want to take advantage under APRAs prudential requirements of the post conversion equity like features of the MEI, then it is likely these instruments would need to meet the same requirements under the Corporations Act as a preference share. (i.e. Part 2H.1 of the Corporations Act.)<sup>25</sup>

4.38 In another example of innovative options for raising capital evolving in the sector, Professor Cotter from Southern Queensland University provided the example of Murray Goulburn issuing units last year:

In terms of capital raising, I think the issue last year of units by Murray Goulburn showed that we do have sufficient flexibility in our legislation for different types of innovative capital raising. However, that is extremely costly, and only the very large co-ops, like Murray Goulburn, could access that. So I think more work needs to be done to make that less costly.<sup>26</sup>

4.39 From the co-operative perspective the Voluntary Parents Services Co-operative expressed their wish for some kind of instrument that would attract capital into co-operatives on the basis of their social-type benefit rather than a financial return:

The situation at the moment is that capital usually comes from a risk basis and people put money into capital on the basis that they might be able to

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25 ASIC, answer to question on Notice, 10 March 2016, p. 4.

26 Professor Julie Cotter, University of Southern Queensland, *Proof Committee Hansard*, 26 February 2016, p. 10.



sell that company for a lot more money than they put into it. The cooperative situation does not have that same benefit because we are not going to sell the company for a whole lot of money. We need to have something like a social bond to provide the facility where it is not based on benefit from risk but benefit for social purpose and that risk matrix is something we have really struggled to find a way to solve to raise capital for social type benefits.<sup>27</sup>

4.40 There are currently limited options for co-operatives and mutuals to raise capital that avoid the debt to equity ratio problem. Ernst and Young explained some of the options available, including the new Cooperative Capital Units developed by CMEs:

CMEs have developed a range of mechanisms to raise capital including Cooperative Capital Units (CCUs) which are flexible instruments determined by members that can include attributes of both debt and equity to attract capital from outside the membership. CCUs can be structured ranging from ordinary debentures to redeemable preference shares. Methods such as proportional voting may be used to raise additional capital from members, but this creates a problem whereby a minority of members may gain control of the cooperative via disproportionate voting rights (28). Alternatively CMEs may look to innovative forms of funding such as crowd sourcing and multi-stakeholder partnerships such as London Ventures.<sup>28</sup>

### *Committee view*

4.41 Central to the committee's concerns is the availability of finance to smaller co-operatives, who cannot raise capital through extensive retained earnings or debt financing. There are a number of innovative practical and policies developing both within the sector and overseas that could assist in providing a suite of options for these organisations. The committee particularly welcomes innovations such as social impact bonds, crowd sourcing and Cooperative Capital Units.

### **Recommendation 15**

4.42 **The committee recommends that Commonwealth and State Governments support the formalisation of some of innovative market-based approaches to raising capital for small and medium sized co-operative and mutual enterprises, in the form of advice and information, as they become available.**

4.43 In terms of improving access to capital for larger mutuals, the committee is aware of the discussions the sector has been having with APRA in respect of changes to legislation and regulations to facilitate easier access to capital. These discussions should properly include an analysis of the applicability of international developments to Australia, as well as the recognition of possible 'hybrid' entities.

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27 Mr David Jordan, Voluntary Parents Services Co-operative, *Committee Hansard*, 29 October 2015, p. 1.

28 Ernst and Young, *Submission 44*, p. 21.

4.44 The committee was concerned to hear that no target date is set for those discussions to culminate, and that no end date is in sight.

### **Recommendation 16**

**4.45 The committee recommends that APRA set a target date for the outcome of discussions with the co-operative and mutuals sector on issues of capital raising and bring those discussions to a timely conclusion.**

4.46 Despite the committee's concern around the delays and administrative delays of the discussions in this area, the committee is cognisant of statements by APRA that 'from an industry perspective, mutuals...are well capitalised'...and 'can grow today if they want to.'<sup>29</sup>

4.47 The committee is of the view that government should not be placing regulatory barriers that impede the development of one sector or another. Furthermore, it is not the role of the government to provide special consideration to one industry or sector. There does seem to be innovation throughout the mutuals sector, as supported by Dr Crane from the BCCM, who said that these innovations 'shows you the way that co-ops and mutuals are trying to work their way through the current either impediments or structures we have around us to find ways to do this'.<sup>30</sup>

4.48 The committee supports this innovation and commends the sector in the efforts they are undertaking to ensure that they are treated equitably. The committee is of the view the government should consider ways to remove any barriers that impede the sector expanding. The evidence the committee received of developments overseas are initiatives that should be examined for applicability in Australia.

### **Recommendation 17**

**4.49 The committee recommends that the Commonwealth Government examine proposals to amend the Corporations Act 2001 to provide co-operative and mutual enterprises with a mechanism to enable access to a broader range of capital raising and investment opportunities.**

**Senator Chris Ketter**

**Chair**

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29 APRA, *Proof Committee Hansard*, 26 February 2016, p. 22.

30 Dr Crane, Business Council of Cooperatives and Mutuals, *Proof Committee Hansard*, 30 October 2016, p. 18.

# **Appendix 1**

## **Submissions and additional information received by the committee**

### **Submissions received**

- 1 Mr Richard Talbot
- 2 Mr Ian Woods
- 3 Confidential
- 4 Mr Greg Patmore
- 5 Bus Association Victoria Inc.
- 6 NRMA
- 7 Cohousing Co-operative Society Limited
- 8 Capricorn Society Limited
- 9 Norco Cooperative Ltd
- 10 International Co-operative Alliance
- 11 Australian Scholarships Group
- 12 Professor Morris Altman
- 13 Dr Branka Krivokapic-Skoko
- 14 Hirmaa
- 15 SouthEast Housing Co-operative
- 16 Co-operation Housing
- 17 National Health Co-op
- 18 Bankmecu
- 19 Mutuo
- 20 Australasian Mutuals Institute
- 21 Defence Bank
- 22 CPSU SPSF
- 23 Employee Ownership Australia and New Zealand
- 24 CPSU
- 25 Industry Super Australia
- 26 Australian Friendly Societies Pharmacies Association Inc
- 27 ME Bank

- 28 Mrs Ann Apps
- 29 Mr Martin Karlsen
- 30 Cooperative Bulk Handling Limited
- 31 Westfund Limited
- 32 Unimutual Limited
- 33 Regis Mutual Management Pty Ltd
- 34 Fleurieu Poultry Association
- 35 Yenda Producers Co-operative Society Ltd
- 36 Dr Gary Lewis
- 37 Voluntary Parents Services Co-operative
- 38 The Co-op
- 39 Customer Owned Banking Association
- 40 Central New South Wales Renewable Energy Co-operative Ltd
- 41 Confidential
- 42 Community Power Agency Co-operative Limited
- 43 Mercury Centre Coop Ltd
- 44 Ernst & Young
- 45 Australian Unity
- 46 MAFIP
- 47 Supporters Direct
- 48 Mr Dominic Kanak
- 49 Friendly Societies of Australia
- 50 National Union of Workers
- 51 Kingfisher Law
- 52 Teachers Mutual Bank
- 53 Credit Union Australia
- 54 Beyond Bank
- 55 Common Equity NSW
- 56 Associate Professor Klaas Woldring
- 57 Ms Robyn Donnelly
- 58 Mr Simon Lane
- 59 Fair Trading, NSW Government
- 60 Master Butchers Cooperative Ltd (MBL)

### **Answers to questions on notice**

- 1      Answers to Questions on Notice by Customer Owned Banking Association at a public hearing held in Sydney, NSW on 29 October 2015
- 2      Answers to Questions on Notice by NRMA at a public hearing held in Sydney, NSW on 29 October 2015
- 3      Answers to Questions on Notice by Business Council of Co-operatives and Mutuals at a public hearing held in Melbourne, VIC on 30 October 2015
- 4      Answers to Questions on Notice by University of Southern Queensland at a public hearing held in Canberra, ACT on 26 February 2016
- 5      Answers to Questions on Notice by National Health Co-op (NHC) at a public hearing held in Canberra, ACT on 26 February 2016
- 6      Answers to Questions on Notice by Consumer Affairs Victoria (Department of Justice) at a public hearing held in Canberra, ACT on 26 February 2016 6 True Edit Delete
- 7      Answer to Question on Notice    Answers to Questions on Notice by Chartered Accountants Australia and New Zealand at a public hearing held in Canberra, ACT on 26 February 2016 7 True Edit Delete
- 8      Answer to Question on Notice    Answers to Questions on Notice by the Australian Taxation Office (ATO) at a public hearing held in Canberra, ACT on 26 February 2016 (1) 8 True Edit Delete
- 9      Answer to Question on Notice    Answers to Questions on Notice by the Australian Taxation Office (ATO) at a public hearing held in Canberra, ACT on 26 February 2016 (2) 9 True Edit Delete
- 10     Answer to Question on Notice    Answers to Questions on Notice by the Australian Competition & Consumer Commission (ACCC) at a public hearing held in Canberra, ACT on 26 February 2016 10 True Edit Delete
- 11     Answer to Question on Notice    Answers to Questions on Notice by the Australian Securities & Investments Commission (ASIC) at a public hearing held in Canberra, ACT on 26 February 2016

**Tabled documents**

- 1 Document tabled by Yenda Producers at a public hearing held in Sydney, NSW on 29 October 2015
- 2 Document tabled by Mr Simon Lane at a public hearing held in Sydney, NSW on 29 October 2015 (1)
- 3 Document tabled by Mr Simon Lane at a public hearing held in Sydney, NSW on 29 October 2015 (2)
- 4 Document tabled by Ms Ellen Michel at a public hearing held in Sydney, NSW on 29 October 2015 (1)
- 5 Document tabled by Ms Ellen Michel at a public hearing held in Sydney, NSW on 29 October 2015 (2)
- 6 Document tabled by Ms Ellen Michel at a public hearing held in Sydney, NSW on 29 October 2015 (3)
- 7 Document tabled by Mr Jeremy Fisher at a public hearing held in Sydney, NSW on 29 October 2015
- 8 Document tabled by Australian Unity at a public hearing held in Melbourne, VIC on 30 October 2015
- 9 Document tabled by Hirmaa at a public hearing held in Melbourne, VIC on 30 October 2015 (1)
- 10 Document tabled by Hirmaa at a public hearing held in Melbourne, VIC on 30 October 2015 (2)

**Additional information**

- 1 Additional Information by Mr Dominic Wy Kanak at a public hearing held in Sydney, NSW on 29 October 2015
- 2 Additional Information by Mercury Centre Coop Ltd at a public hearing held in Sydney, NSW on 29 October 2015 (1)
- 3 Additional Information by Mercury Centre Coop Ltd at a public hearing held in Sydney, NSW on 29 October 2015 (2)
- 4 Additional Information by Mercury Centre Coop Ltd at a public hearing held in Sydney, NSW on 29 October 2015 (3)
- 5 Additional Information by Mr Zachary May at a public hearing held in Melbourne, VIC on 30 October 2015





## Appendix 2

### Public hearings

*Sydney NSW, 29 October 2015*

**Members in attendance:** Senators McKenzie, Xenophon

**Witnesses**

BRADBERRY, Dr Patrick James, Director, Central New South Wales Renewable Energy Co-operative Ltd

CALABRIA, Mr Peter John, Managing Director, Yenda Producers Co-operative

CRONAN, Mr Garry, Board Member, Mercury Centre Cooperative Ltd

DALTON, Mr Nayce, Deputy Chairman, Yenda Producers Co-operative

DEGOTARDI, Mr Mark, CEO, Customer Owned Banking Association

DONNELLY, Ms Robyn Anne, Private capacity

FISHER, Mr Jeremy Lawrence, Private capacity

FOGARTY, Mr Martin John, Director, Voluntary Parents Services Co-operative

JORDAN, Mr David Humphrey, Chairman, Voluntary Parents Services Co-operative

KNOCK, Mr Peter, Chief Executive Officer, The Co-op

LANE, Mr Simon Thomas, Chairman, Almondco Australia Pty Ltd

LEWIS, Dr Gary, Private capacity

MACHIN, Ms Wendy, Deputy President, National Roads and Motorists' Association

MacKENZIE, Ms Sally, Senior Policy Adviser, Customer Owned Banking Association

MATHIE, Mr James Paul, Head of Club Development, Supporters Direct

McFARLANE, Mr Terry, Chairman, Yenda Producers Co-operative

MICHEL, Ms Ellen, Executive Director, Cooperative Grocer Network

NOCKOLDS, Mr Tom, Director, Community Power Agency Co-operative Ltd

PATMORE, Professor Gregory Edward, Private capacity

TREGILGAS, Mr Peter Frank, Chair, Mercury Centre Cooperative Ltd

VAN DER LOOS, Rene Ms, General Manager, Living Well Navigator, National Roads and Motorists' Association

WYKANAK, Mr Dominic, Private capacity

***Melbourne VIC, 30 October 2015*****Members in attendance:** Senators McAllister, McKenzie, Xenophon**Witnesses**

BATT, Ms Karen, Federal Secretary, Joint National Secretary, Community and Public Sector Union

CHIU, Mr Osmond, Research Officer, Community and Public Sector Union

CRANE, Dr Andrew, Chairman, Business Council of Co-operatives and Mutuals; and Chief Executive Officer, Co-operative Bulk Handling Limited

FISHER, Mr Michael, Policy Analyst-Regulatory Policy, Industry Super Australia

GREEN, Dame Pauline, President, International Co-operative Alliance

GRIFFITHS, Mr David Henry, Acting Manager (Governance), SouthEast Housing Co-operative Ltd

HAINES, Ms Joy, Acting Manager (Operations), SouthEast Housing Co-operative Ltd

HUNT, Mr Peter, Managing Partner, Mutuo

KOCE, Mr Matthew, Chief Executive Officer, hirmaa

LOWE, Mr Chris, Executive Director, Bus Association Victoria

MAY, Mr Zachary, Director of Policy, Industry Super Australia

McCOY, Mr Kevin, Chief Financial Officer, Australian Unity

McMILLAN, Mr Derek, Chief Executive Officer, Retirement Living, Australian Unity

MEAD, Mr Rohan, Group Managing Director, Australian Unity

MORRISON, Ms Melina Josephine, Chief Executive Officer, Business Council of Co-operatives and Mutuals

PERICA, Mr Mark Damian, Senior Legal Officer, Community and Public Sector Union

SEDICK, Mr Kemal (Kim), Chief Executive Officer, Rumbalara Aboriginal Co-operative

VAN BARNEVELD, Dr Kristin, Director of Research, Community and Public Sector Union

VELEGRINIS, Mr John, Chief Executive Officer, Australian Scholarships Group

WALL, Mr Gregory Joseph, Director, International Co-operative Alliance

WALSH, Mr Matthew, President, Friendly Societies of Australia

***Canberra ACT, 26 February 2016***

**Members in attendance:** Senators Ketter, McKenzie, Xenophon

**Witnesses**

BRENNAN, Mr Pat, General Manager, Policy Development, Australian Prudential Regulation Authority

COTTER, Professor Julie, Director, Australian Centre for Sustainable Business and Development, University of Southern Queensland

GREEN, Mr Chris, Senior Manager and Regional Commissioner for Tasmania, Australian Securities and Investments Commission

O'ROURKE, Ms Kate, Senior Executive Leader, Corporations, Australian Securities and Investments Commission

POULAKIS, Mr Tony, Assistant Commissioner, Private Groups and High Wealth Individuals, Australian Taxation Office

SQUIRES, Ms Katrina, Senior Manager, Policy Development, Australian Prudential Regulation Authority

WATTS, Mr Adrian, Managing Director, National Health Co-op Ltd

WILSON, Mr Blake, Acting Chairman, National Health Co-op Ltd

