



BUSINESS COUNCIL
OF CO-OPERATIVES AND MUTUALS

Submission to the Parliamentary Joint Committee on
Corporations and Financial Services

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About the BCCM

Formed in 2013 following the United Nations International Year of Co-operatives¹, the Business Council of Co-operatives and Mutuals (BCCM) is the peak body for Australian co-operatives, mutuals and member-owned enterprises. The BCCM represents a diverse range of enterprises operating in sectors including agriculture, finance and banking, insurance, motoring services, health services, aged care, disability employment, education, indigenous services, social housing and retail.

The BCCM advocates for recognition of the sector and for measures that create a level playing field between co-operatives and other businesses, including implementation of the recommendations of the Senate Economics References Committee report into Cooperative, mutual and member-owned firms², and implementation of the Hammond review into Access to Capital for CMEs.³

¹ See <https://social.un.org/coopsyear/>

² http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Cooperatives/Report

³ <https://treasury.gov.au/publication/p2017-t235882/>

1 Introduction

The Business Council of Co-operatives and Mutuals (BCCM) welcomes the opportunity to provide a submission to the Parliamentary Joint Committee on Corporations and Financial Services inquiry into the operation and effectiveness of the Franchising Code of Conduct.

Our submission provides information about the significant enterprise co-operative sector that operates in many of the same markets as franchise businesses. We argue that alongside consideration of franchise regulation, this inquiry should consider the broader policies designed to promote business diversity in small business and franchise markets. In so doing, **our submission responds to term of reference (h), any related matter.**

The BCCM would be pleased to attend a hearing to answer any questions the Committee may have about the matters raised in our submission.

2 Response to Terms of Reference

(h) any related matter.

1.1 This inquiry should recognise the significant enterprise co-operative sector that operates in the same markets as franchise businesses

Co-operatives exist when groups of individuals or businesses come together to achieve an objective that they could not achieve alone. They are a rational alternative to investor-owned businesses when the objective is different from maximising returns to shareholders. Co-operatives are often formed as a response to the failure of a market to adequately serve the interests of a group of customers, workers or producers (enterprises). Because the co-operative business purpose is different, these firms behave differently, pursuing business plans that aim to secure long term success for their members.

In enterprise co-operatives⁴, member-businesses voluntarily pool their resources to achieve efficiencies while maintaining local ownership, control, identity and benefit. In a co-operative, head office becomes the support office. Enterprise co-operatives are global in their reach, as examples like CarpetOne, Best Western, and Australia's own Capricorn Society, attest.⁵

Like franchisors, many enterprise co-operatives develop common branding and group buying services. Enterprise co-operatives are democratically guided by members in setting such a strategy and undertake such activities for the benefit of and at the behest of members. The enterprise co-operative structure avoids the perverse incentive of top-down models such as price gouging. As Professor Morris Altman notes, 'The traditional investor-led model is not the only viable organizational model. There is a co-operative alternative that can be equally or even more viable whilst generating *more* equitable outcomes to franchisees and also to the customers of the franchisors.'⁶

Examples of enterprise co-operatives of retailers that incorporate a common marketing or branding

⁴ For a taxonomy of the types of enterprise co-operative see: http://bccm.coop/wp/wp-content/uploads/2014/05/BCCM-submission-to-SBO_FIN.pdf, 17.

⁵ CarpetOne and Best Western are global in reach. Capricorn Society operates across Australia and New Zealand. <https://www.carpetone.com.au/>; <http://joinbestwestern.com/>; <https://www.capricorn.coop/?Country=JP>

⁶ Full abstract included as appendix B

strategy include:

- RapidClean Group (more than 50 cleaning supply stores around Australia);⁷
- Independent Liquor Group (wholesale and logistics for independent liquor stores across NSW, ACT and QLD, undertakes some common branding programs);⁸
- Tyrepower (260 independent tyre retailers using common branding);⁹
- CarpetOne (global independent carpet and flooring retailers' co-operative with 45 Australian members);¹⁰
- Best Western (association of 4,200 independently owned and operated hotels globally, including 180 in Australia and New Zealand);¹¹
- Go Vita (more than 150 health food stores around Australia);¹²
- Associated Retailers Limited (supports more than 500 general retailers with branding and buying support);¹³
- Tasmanian Independent Retailers Co-operative (TIR gives access to the IGA brand to 80 member retailers in Tasmania);¹⁴
- Liquor Barons Co-operative (55 Western Australian independent liquor stores using common branding);¹⁵ and
- Furniture One (33 independent furniture retailers using common branding in New South Wales).¹⁶

The enterprise co-operative structure is flexible and can be found undertaking a diverse range of activities in different sectors outside of retail:

- Capricorn Society, owned by 18,000 independent mechanics and crash repairers, focuses on group buying and insurance and risk services for members in Australia and New Zealand;¹⁷
- Almondco undertakes processing and marketing of almonds for 85% of Australia's almond growers;¹⁸
- Travellers Choice, a co-operative of independent travel agents, undertakes group buying, networking and marketing support activities for the benefit of member travel agents;¹⁹
- Master Butchers Co-operative provides supplies and undertakes manufacturing of meat products for the benefit of member-businesses;²⁰ and
- Plumbers' Supplies Co-op gives member-businesses access to supplies at the best price.²¹

⁷ <http://rapidclean.com.au/>

⁸ <http://www.ilg.com.au/>

⁹ <https://www.tyrepower.com.au/>

¹⁰ <https://www.carpetone.com.au/>

¹¹ <http://joinbestwestern.com/>

¹² <http://www.govita.com.au/>

¹³ <http://www.arl.com.au/>

¹⁴ <https://tir.com.au/>

¹⁵ <https://www.liquorbarons.com.au/about-us/>

¹⁶ <https://furnitureone.com.au/store-finder.php>

¹⁷ <https://www.capricorn.coop/?Country=JP>

¹⁸ <http://www.almondco.com.au/>

¹⁹ <https://www.travellerschoice.com.au/agents>

²⁰ <https://www.mblsa.com.au/>

²¹ <https://www.pscoop.com.au/>

1.2 How enterprise co-operatives enhance the competitiveness of small businesses and improve the functionality of markets they operate in

The BCCM submits that policies which promote business model diversity should be considered alongside regulation as a means of achieving the aim of sustainable, functional markets and competitive and viable small businesses and franchises. Enterprise co-operatives can support public policy objectives in the following ways:

The presence of enterprise co-operatives in markets increases corporate diversity, reducing systemic risk for the community from business model failures

The financial sector is one area (due to its systemic impact) where, since the GFC, corporate monoculture has been increasingly acknowledged by policymakers. In his study of the performance of European financial institutions following the GFC, Birchall found that co-operative banks acted counter-cyclically, increasing the resilience of the economy as a whole.²² Canadian studies have demonstrated that the failure rate for co-operatives is significantly lower than for other firms, demonstrating their stability as a business model.²³ A diverse private sector reduces the chance of systemic failures that can prompt large and expensive policy interventions.

Enterprise co-operatives provide competition and choice for consumers (i.e. for small businesses and franchisees purchasing goods and services)

Customer-owned enterprises like mutual health insurers can drive price and quality competition for the benefit of consumers, whether they are members or non-members. Mutual health insurers return a higher percentage of premiums as benefits to members than for-profit insurers.²⁴ As a result of the existence of different business models in the market, there is permanent competitive pressure placed on profit-maximising firms operating in that market.

Small businesses, like individual customers, benefit from the existence of a diversity of business models in the markets they purchase services in. In particular, the presence of enterprise-owned service providers can drive price and quality rivalry, to the benefit of members and non-members in that market. The Harper Review into Competition Policy Final Report acknowledged that increased awareness and uptake of co-operative models would 'potentially strengthen the bargaining position of small businesses dealing with large businesses.'²⁵

Additionally, the presence of diverse and innovative models can give new and existing entrepreneurs greater choice in the types of 'strategic networks' from which they gain access to goods and services.²⁶ Two examples of franchisees exiting a franchise system to form an enterprise co-operative in the United States are KaleidoScoops (from Baskin-Robbins), and Donut Connection (from Dunkin' Donuts).²⁷

²² http://www.ilo.org/wcmsp5/groups/public/---ed_emp/---emp_ent/---coop/documents/publication/wcms_207768.pdf

²³ http://www.uwcc.wisc.edu/pdf/BALTA_A11_report_BC.pdf

²⁴ <https://www.smh.com.au/business/consumer-affairs/new-figures-show-notforprofit-health-fund-members-get-more-for-their-money-20170329-gv8ymv.html>

²⁵ <http://competitionpolicyreview.gov.au/final-report/>

²⁶ See http://bccm.coop/wp/wp-content/uploads/2014/05/BCCM-submission-to-SBO_FIN.pdf, 17.

²⁷ <https://www.entrepreneur.com/article/224765>

Enterprise co-operatives support the long-term viability of their small business members

The vast majority (over nine in ten) of Australian businesses are small businesses; they account for 33 per cent of Australia's GDP and employ over 40 per cent of Australia's workforce.²⁸ The potential role of enterprise co-operatives in driving productivity and profitability is therefore enormous.

The ability of enterprise co-operative models to increase member profitability and sustainability has been recognised in the agricultural sector, where the Agricultural Competitiveness White Paper noted that '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.'²⁹ Howard Brodsky, Chair of United States enterprise co-operative, CCA Partners, reported that while '25 percent of independent flooring shops bit the dust during the [GFC], CCA flooring cooperatives had a failure rate between 1 and 2 percent.'³⁰ Professor Altman suggests that the '[n]atural and common preferences against self-harm (a key component of the co-operative organizational form) incentivize the co-operative franchise to focus on the long run viability of the franchisee and franchisor.'³¹

Enterprise co-operatives share the benefits of business with employees and the community

Enterprise co-operative don't just benefit their small business members. Enterprise co-operatives strengthen local economies through the long-term retention of local small businesses and jobs.³² The McClure Review noted that 'in developing intergenerational self-reliance, co-operatives help to reduce welfare dependency... provide jobs for local people, offer goods and services and use procurement practices that support local business'³³ Professor Altman suggests that 'the co-operative franchise can make a lot of money (surplus over core costs), but also use components of the surplus to benefit community and employees—part of the co-operative organizational principles.'³⁴

3 Recommendations

Co-operatives need a level playing field with other forms of enterprise if they are to form and grow, as was recognised by the Senate Economics References Committee in its report in the inquiry into cooperative, mutual and member-owned firms.³⁵ The implementation of the recommendations arising from that inquiry is the basis for co-operatives being able to contribute more to Australian community and economic life into the future, including in the small business and franchise sector.

²⁸ http://www.asbfeo.gov.au/sites/default/files/Small_Business_Statistical_Report-Final.pdf , 6.

²⁹ <http://agwhitepaper.agriculture.gov.au/SiteCollectionDocuments/ag-competitiveness-white-paper.pdf> ,28.

³⁰ <https://www.entrepreneur.com/article/224765>

³¹ See appendix B

³² http://bccm.coop/wp/wp-content/uploads/2014/12/Sticky-Money-Report_EY-2014.pdf

³³ https://www.dss.gov.au/sites/default/files/documents/02_2015/dss001_14_final_report_access_2.pdf , 181.

³⁴ See appendix B

³⁵ Commonwealth of Australia (2016) *Report of the Senate Economics Reference Committee Inquiry into Cooperative, Mutual and Member- Owned Firms*.

Therefore, the BCCM recommends:

1. Implementation of all 17 recommendations of the Senate Economics References Committee inquiry into cooperative, mutual and member-owned firms.³⁶

We note also that ILO Recommendation 193 on the “Promotion of Co-operatives”³⁷ sets out principles for how government should work with the co-operative and mutual sector to promote its growth:

- Co-operatives, mutual 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 on an equal basis alongside other types of corporate ownership
- Government should recognise the value of these businesses and provide appropriate incentives for their creation and development
- Legislation and regulation for these firms should match the best practice for any business, and
- It should be cost effective and straight forward to set up and run co-operative, mutual or member-based businesses as any other type of business.

The greatest barrier for the uptake of innovative enterprise co-operative models is awareness among small business owners and their advisors. In relation to enterprise co-operatives we therefore recommend the additional following action in line with Recommendation 7 of the Senate Economics References Committee inquiry into cooperative, mutual and member-owned firms:

2. A time-limited program with the objective of building legacy information and resources for government agencies and services that deliver small business and enterprise development services. This program should be delivered in partnership with the co-operative and mutual sector.

³⁶ See Appendix C

³⁷ Recommendation concerning Promotion of Co-operatives, Adoption: Geneva, 90th ILC Session (20 June 2002)
http://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:12100:0::NO::P12100_ILO_CODE:R193

4 Appendix A: what are co-operative and mutual enterprises (CMEs)?

Co-operative and mutual enterprises (CMEs) are businesses owned by or on behalf of their customers, employees, a group of like-minded producers or a combination of these.

CMEs are self-help enterprises that form to meet the common economic and social needs of a group of people or businesses. Often the group's needs are not being met due to various kinds of market failure.

There are 1.2 billion members of co-operatives globally.³⁸ In Australia there are more than 2,000 co-operatives and mutuals with a combined membership base of more than 14.8 million.³⁹

Co-operatives are guided by seven internationally-agreed principles (incorporated into Australian law through the Co-operatives National Law⁴⁰):

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.

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.

³⁸ For this and other global statistics about the co-operative movement, see <https://ica.coop/en/facts-and-figures>

³⁹ <http://bccm.coop/wp/wp-content/uploads/2017/11/BCCM-2017-NME-Report.pdf>

⁴⁰

http://www.fairtrading.nsw.gov.au/ftw/Cooperatives_and_associations/About_cooperatives/Cooperatives_national_law.page

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.

Broadly speaking, there are three types of co-operative and mutual enterprise – customer owned, worker owned and producer owned - that deliver sustainable production of goods and services to the key stakeholders

Customer owned: The objective is service quality and price, rather than profit maximisation. Australian examples including customer-owned banks (e.g. CUA, Bank Australia), health insurance (HCF, RT Health), food retail (The Co-op - Barossa), primary health (National Health Co-operative) and motoring clubs (RACQ, NRMA).

Worker owned: The objective is high quality employment that incentivises employees, provides work place democracy and shares wealth, often whilst pursuing social goals like high quality social care and environmental health. Australian examples are non-residential aged care provider, The Co-operative Life, and refuse shop operator, Resource Work Cooperative.

Producer owned: The objective is to enable groups of small businesses to work together to operate in markets that they could not enter alone or would otherwise be dominated by large investor owned firms. Many such co-ops exist in agricultural production, where co-ops enable smaller producers to combine their efforts to compete. Well known examples are Co-operative Bulk Handling (CBH) and dairy-farmer owned Norco Co-operative, and in automotive purchasing, Capricorn Society.

5 Appendix B: Co-operative versus Investor-Led Franchises

Co-operative Versus Investor-Led Franchises: Wherein Lies the Co-operative Advantage?

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Abstract: The argument presented here is that there are different models of franchising. The traditional investor-led model is not the only viable organizational model. There is a co-operative alternative that can be equally or even more viable whilst generating *more* equitable outcomes to franchisees and also to the customers of the franchisors. Franchising (with the focus on the investor-led model) *lends the appearance* of being fair and equitable as well as economically viable alternative to erstwhile prospective entrepreneurs and current small and medium sized businesses who might be unable to compete with large firms that can take advantage of economies of scale in production and in input purchasing (supply chain) as well as in quality control and pricing. In theory, a franchise can mimic the large firm without closing the door to prospective entrepreneurs (barriers to entry) and without forcing the exit of existing small to medium sized firm. The traditional franchising model is perceived as investor-led wherein a large corporation (firm) franchises licensees (franchisees) to produce or sell goods and/or services under a certain brand name. In this model, the objective of the exercise is for is for large corporation which is the franchisor to maximize its profits. And, if this large corporation is controlled by an investment fund focusing on short run returns, the focus is on incentivizing the franchisee to maximize short run returns even if it is at the cost of product quality, employee income and overall wellbeing, and the long run viability of the franchisee. This is known as the paradox of the franchise model wherein the brand is sacrificed for short run economic gain.

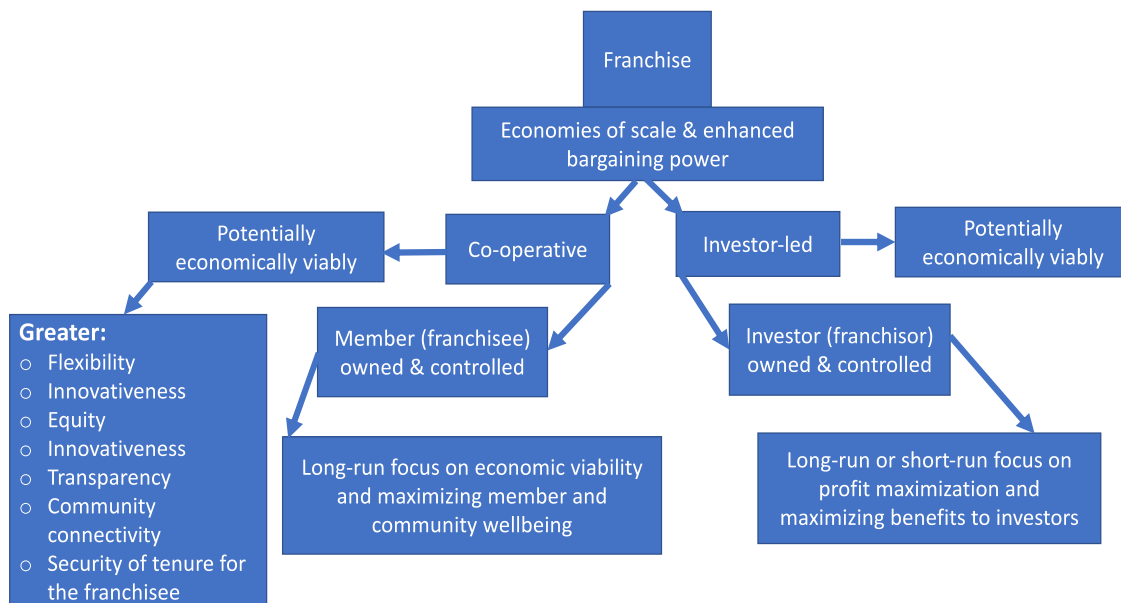
In the co-operative model, the franchise is built bottom-up by the franchisees who are member-owners of the franchise. The franchisee is also the franchisor. In the co-operative model the incentive is to maintain and develop the long run economic viability of the franchise and the larger franchise organization. Because the owner of franchise is also one of the owners of the larger franchise corporation, there is no incentive for the larger franchise to cause harm to the franchisee. Natural and common preferences against self-harm (a key component of the co-operative organizational form) incentivize the co-operative franchise to focus on the long run viability of the franchisee and franchisor.

Moreover, in the co-operative model, the franchisee member-owners, build the franchise in a manner that suits their self-interest in the context of local conditions (as compared to the investor-owned model), hence lending itself to more flexibility and innovativeness. Its focus is on economic viability, which is not the same thing as profit maximization. The co-operative

franchise can make a lot of money (surplus over core costs), but also use components of the surplus to benefit community and employees—part of the co-operative organizational principles. Moreover, transparency is also part and parcel of co-operative organizational principle and key to co-operative success. In the co-operative model, there are the same benefits accruing from networking related economies of scale and bargaining power (as in the investor-owned model). But in the co-operative model, the benefits accrue to owner-members, not to the investor owners as in the investor-led model. Additionally, there is greater security of tenure to the franchisee. In the investor-led model, there is a positive probability of non-renewal, which can sometimes be quite significant, which creates a less positive incentive environment for the franchisee.

This type of equity, along with lending itself to greater flexibility, bottom-up innovativeness, transparency, and concern for community are key to the co-operative advantage in franchising even in the most competitive of market economies.

Different Franchise Organizational Forms



6 Appendix C: Recommendations of the Senate Economics References Committee inquiry into cooperative, mutual and member-owned firms

Recommendation 1

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

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

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

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

Recommendation 5

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

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

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

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

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

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

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

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

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

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

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

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

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.